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SHARES

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WHAT TO DO WITH YOUR INVESTMENTS

EXPERTS PICK THEIR FAVOURITE FUNDS THAT PAY DIVIDENDS **EVERY MONTH**

WHY WE ARE **BULLISH** ON VODAFONE AND ROYAL MAIL

ENERGY PRICE CAP: WHAT IT MEANS FOR CENTRICA'S EARNINGS

How to spot trouble brewing with one of your investments

We reveal three words in trading updates which could point to problems ahead

A shock profit warning and share suspension from toilet roll maker **Accrol (ACRL:AIM)** provides a timely reminder to look for negative signs in trading updates.

It was impossible to spot all the negative points that led to Accrol saying current year earnings would be significantly below market forecasts and that net debt had ballooned.

However, there were two signs in the previous trading update (published on 7 September) which raised the risks associated with holding the shares. Investors would do well to study Accrol's situation and apply the red flag research methodology to other shares.

RECENT WARNING SIGNS

Accrol's 7 September update said profitability was 'broadly' in line with market expectation. That's your first red flag. 'Broadly' is a term often used by companies to essentially mean below expectations, but not severe enough for analysts to make significant downgrades to their earnings models. In reality it means things aren't going well.

The second red flag was the sudden departure of the chief executive to 'pursue other interests'. Company bosses don't suddenly walk out unless there has been a problem or a disagreement over strategy. The CEO would certainly need to work out their notice period if they'd found another job.

Negative signs in trading updates

The combination of wobbly trading guidance and the CEO disappearing provided a double whammy of red flags and made Accrol very vulnerable to share price declines until it gave more clarity on matters.

Anyone reading the company's AIM admission document from June 2016 would have seen reference to currency dangers. It flagged that the business would be negatively impacted if pound sterling depreciated in value against overseas currencies, as it buys most of its paper in US dollars and euros.

Sterling did weaken in the aftermath of Accrol joining the stock market – but it has also recovered strongly this year. That might be why some investors were happy to hold on to the shares.

Accrol announcing a new CEO at the same time as saying the old one was going implied the company was merely bringing in new blood – and one with experience of a FTSE 250 business, namely packaging group **DS Smith (SMDS)**.

Furthermore, many companies use the term 'broadly' in line, when referring to trading – and subsequently don't issue a profit warning. In hindsight, I can see why some investors didn't spot problems with Accrol. Yet perhaps it has taught us a lesson to not be so forgiving when red flags appear.

LUCKY ESCAPE

Premier Asset Management fund manager Chris White told me that he sold the final tranche of Accrol shares from his income portfolio on the day before last week's profit warning.

One of his colleagues had flagged the business as the most likely stock in Premier's portfolio to issue a profit warning due to a variety of factors, so the fund manager dumped the stock.

You can look for risks to an investment case by using certain search terms on websites that contain official stock market announcements. For example, go to https://investegate.co.uk/ , highlight 'Keyword' above the search field and type in either 'broadly', 'challenging' or 'weakened'.

That will help you spot companies potentially in trouble. Examples of stocks recently using these words include **Filtronic (FTC:AIM)**, **Capita (CPI)**, **Topps Tiles (TPT)** and **Greene King (GNK)**. (DC)

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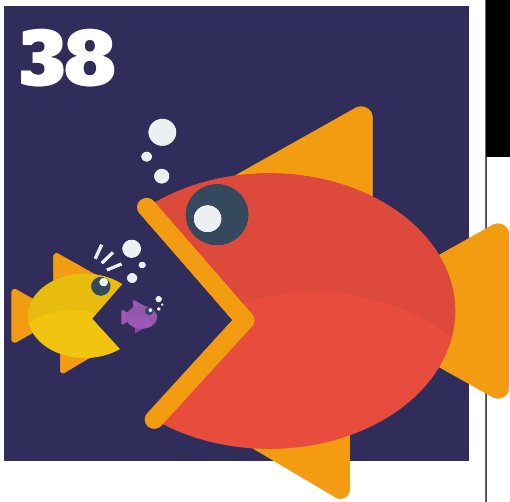

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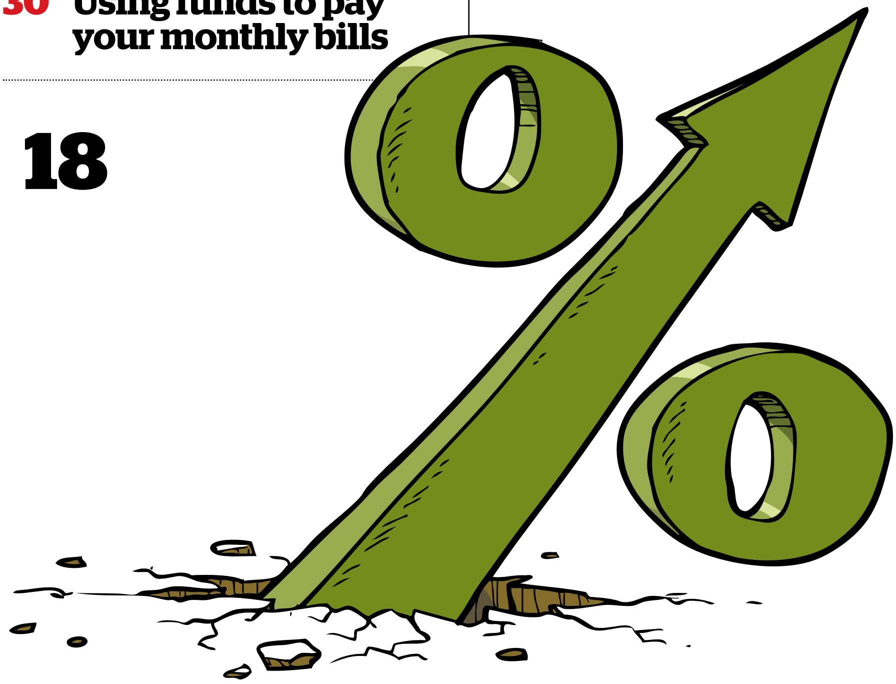

WHO WE ARE

EDITOR: Daniel Coatsworth @SharesMagDan

DEPUTY EDITOR: Tom Sieber @SharesMagTom

NEWS EDITOR: Steven Frazer @SharesMagSteve

FUNDS AND INVESTMENT TRUSTS EDITOR: James Crux @SharesMagJames

REPORTER: David Stevenson @SharesMagDavid

JUNIOR REPORTER: Lisa-Marie Janes @SharesMagLisaMJ

CONTRIBUTORS Emily Perryman, Tom Selby

PRODUCTION
Head of Design: Rebecca Bodi
Designer: Darren Rapley

ADVERTISING
Sales Executive: Nick Frankland
020 7378 4592
nick.frankland@sharesmagazine.co.uk

MANAGING DIRECTOR
Mike Boydell

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BROKER RATINGS EXPLAINED:

We use traffic light symbols in the magazine to illustrate broker views on stocks.

Green means buy, Orange means hold, Red means sell.

The numbers refer to how many different brokers have that rating.

Eg: 4 2 1 means four brokers have buy ratings, two brokers have hold ratings and one broker has a sell rating.

The traffic light system gives an illustration of market views but isn't always a fully comprehensive list of ratings as some banks/stockbrokers don't publicly release this information.

Energy price cap threatens Centrica's earnings and dividend

That's bad news for one of the FTSE's most popular income stocks

The Government has confirmed plans to introduce energy price caps across what prime minister Theresa May has called 'the broken energy market.'

The news prompted a steep decline in the share price of **Centrica (CNA)** which looks likely to be worst hit by an Ofgem clampdown. It has also called into question the group's future dividend payout plans, the main reason investors hold the shares.

The stock has fallen roughly 10% to 173.9p.

Centrica owns British Gas, by far the biggest single gas and electricity supplier to UK homes, with estimated respective market shares of 34% and 22%, according to Ofgem data.

The price cap 'might cost Centrica something like £200m' a year, calculates Neil Wilson, market analyst at ETX Capital. That figure chimes with previous estimates from investment bank UBS of 'a reduction of £150m to £200m per annum or approximately one-third of Centrica's UK supply margins'.

Profitable standard variable rate tariffs will come under attack by the energy watchdog.

Like other providers Centrica relies heavily on these standard variable rate tariffs with 'about three-quarters of customers on these lucrative contracts,' estimates ETX's Wilson.

In 2016 Centrica reported £1.47bn operating profit from which it paid out £533m in dividends. This year the market anticipates roughly the same dividend on lower operating profit of £1.43bn.

Centrica was forced to cut its dividend by 30% between 2013 and 2015 to 12p per share, a level at which it has remained. The company had hoped to return to a 'progressive' payout policy going forward, but those plans may now have to be put on hold. (SF)

Christmas comes early for Cranswick

PREMIUM PORK-TO-POULTRY play **Cranswick (CWK)** is a likely beneficiary of the problems facing leading poultry processor 2 Sisters, which is under investigation by the UK Food Standards Agency for potential food safety standard breaches. Supermarkets including **Sainsbury's (SBRY)**, Lidl and **Marks & Spencer (MKS)** have suspended supplies from the plant under investigation at a time when Cranswick is winning cooked chicken contracts and doubling poultry processing capacity. (JC)

Online orders heat up Domino's shares

TAKEAWAY FRANCHISE **Domino's Pizza (DOM)** saw its shares rally more than 10% to 342.5p on 10 October after reporting a 21% increase in group sales in the third quarter, supported by rising online orders and cutting prices for those whose buy two or more pizzas.

Digital sales in the UK were up 17.4% in the period. The company is sticking with its plans to open 90 new UK stores in 2017. (TS)

Capita announces new CEO

FORMER AMEC Foster Wheeler boss Jon Lewis is joining outsourcer **Capita (CPI)** as CEO.

The company had been without a chief executive since Andy Parker announced he was leaving in March and stepped down last month.

Parker had a tricky tenure with a string of profit warnings as well as disputes with staff over pension changes. Lewis will join on 1 December, allowing interim chief executive Nick Greatorex to return to his role as finance director. (DS)

Where next for the UK stock market?

Taking the temperature of stocks heading into the final months of 2017

THE FTSE 100 remains in touching distance of record highs but there is still considerable uncertainty over the Brexit process and the looming issue of a UK interest rate rise – possibly as early as next month (2 Nov).

Canaccord Genuity says investors should consider the relative underperformance of UK shares against other global benchmarks when considering where the market is headed next.

The Canaccord team notes the FTSE All-Share is only up by 12% over the last 12 months against the US S&P 500 up 21% and the Euro Stoxx up 23% despite the benefit from weaker sterling and the strong performance of mining stocks which are more heavily represented in the UK than elsewhere.

UK stock market is lagging its US and European peers

They suggest this situation implies there is already a high level of political/economic risk embedded within both the broad UK market, and the mid-market specifically.

'With political risk not obviously lower in other industrial markets, we don't see this underperformance as merited'.

Overall, they see the UK market as being in 'good health' with solid performance, a decent economic backdrop and valuations a little on the high side but 'within normal ranges'.

The main risks identified are a deterioration of the political situation and weak growth in wages. (TS)

Can exploration make a comeback after North Sea oil discovery?

Second-time lucky for Jersey Oil & Gas on Verbier prospect

EXCITEMENT CONTINUES to build at North Sea oil explorer **Jersey Oil & Gas (JOG:AIM)** after a well on its 18%-owned Verbier prospect identified up to 130m barrels of oil.

Drilled with Norwegian operator Statoil, this side-track well involved re-entering a previously unsuccessful well from its surface location but then changing direction to target a different area of the sub-surface.

Preliminary results suggest the find could contain anywhere between 25m and 130m barrels of oil and the result could reignite investor interest in exploration stocks both in the North Sea and further afield.

Over-capacity of drilling rigs has brought exploration costs down considerably. The chief executive of **Eco Atlantic Oil & Gas (ECO:AIM)** Gil Hozman tells *Shares* he hopes this will mean activity on its Orinduik block offshore Guyana will be accelerated, though the pace will ultimately be dictated by **Tullow Oil (TLW)** which has a 60% stake and is the operator.

There has been considerable excitement offshore Guyana thanks to ExxonMobil's multi-billion barrel Liza discovery in 2015 which lies 6.5 kilometres from Orinduik.

Eco Atlantic recently inked an option agreement with Total on the block which could see the French oil major take a 25% stake, leaving Eco with 15%. In return Total will pay up to $13.5m which should fund Eco's share of two wells on Orinduik.

Total has four months to study recently acquired seismic data before committing and Hozman says on the current timetable that would imply a decision in April 2018. In the interim he says there is likely to be near-term news flow affecting its assets offshore Namibia. (TS)

Polar launches new megatrends fund

Automation and artificial intelligence are key long-term themes

Investment company **Polar Capital (POLR:AIM)** has launched a new technology megatrends fund. **Polar Capital Automation and Artificial Intelligence Fund** will focus on four powerful secular themes: industrial automation, artificial intelligence (AI), robotics and materials science.

Fund manager Ben Rogoff believes the next three to five years will spark a period of massive disruption capable of 'unlocking significant value for investors'.

'Intelligent machines will require a rewriting of fundamental design and manufacturing principles,' he says. 'We believe this could prove as significant as the introduction of just-in-time inventory management and the reinvention of logistics in the 1980s.'

The fund plans to invest in between 50 and 80 companies from around the world and across the market size spectrum. Its target is to deliver superior returns for investors above the MSCI ACWI benchmark index which has risen by nearly 50% over the past five years.

Retail investors will incur a 1.3% annual management charge.

Polar Capital Automation and Artificial Intelligence Fund will have a more specific investment remit than the asset manager's existing technology vehicles.

These include **Polar Capital Technology Investment Trust (PCT)** and **Polar Capital Global Technology Fund (IE00B42W4J83)**, which have £1.8bn and $1.6bn of assets under management respectively. (SF)

Streamlined BAE aims to fly

Defence giant set to cut jobs to remain competitive

DEFENCE BEHEMOTH **BAE (BA.)** is planning to make job cuts across three divisions to improve efficiency, operational effectiveness and 'drive competitiveness'.

The division most impacted by this streamlining programme is the military air and information business which is set to cull 1,400 roles. The company says these actions are needed as production of both its Eurofighter Typhoon jet and its Hawk training jet winds down.

While BAE recently got a lift from a letter of intent to buy 24 Typhoon jets and six Hawks by Qatar, a lack of certainty over future orders has prompted the action.

A further 375 jobs in maritime services and 150 in cyber intelligence are set to go.

Berenberg analyst Charlotte Keyworth foresaw a need to address issues with Typhoon programme in a piece of research on 2 October.

Downgrading the stock from 'buy' to 'hold', she noted that in the absence of a firm export order materialising for the Typhoon, 'we now forecast full year 2018 and 2019 delivery rates falling around 50% year-on-year from 20 in 2017 to 11 and five aircraft respectively'.

Business is set to cull 1,400 roles

This is the first definitive cost cutting move by BAE's chief executive Charles Woodburn, who took over in July. He reiterates guidance for underlying earnings per share for 2017 to be 5% to 10% higher than 2016's figure of 40.3p and is also expecting a small reduction in net debt.

Commenting on the update Citibank says: 'BAE Systems is a resilient business that we believe can weather bumps in the road (such as these redundancy/reorganization charges) and still meet expectations, supported by 3.6% dividend yield.' (DS)

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The fund is independently rated by RSM and "A" rated by Square Mile Research. TB Saracen Global Income and Growth Fund has an active share of over 90%.

The fund has been ranked first quartile over one year and second quartile over five years.

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Click **here** to find out more information

[1] Based on 4.27p per share on Income shares for 2016

[2] HI 2017 rate was 3.94p per share.

Fund Performance since inception (from 06/11 – 09/17)

Source: Financial Express

Total Return, Bid to Bid, GBP terms. Past performance is not a reliable indicator of future results. The value of your investment and the income derived from it can go down as well as up and you may not get back the money you invested.

Fund has been selected as part of the **AJ Bell Favourite Fund List 2017**

AJ BELL FAVOURITE FUND LIST 2017

Cumulative Performance after all ongoing charges to 29th September 2017

	1 month	6 months	1 year	3 years	5 years	Since launch[1]
TB SGIG B Acc	+0.4%	+2.2%	+19.1%	+44.8%	+91.7%	+104.5%
Sector Average	-1.3%	+1.4%	+12.3%	+36.2%	+73.8%	+81.6%
Quartile Ranking	1	2	1	2	1	1

[1]Source: Financial Express; launch date 07 June 2011
Sector: IA Sector (Global Equity Income)

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24.7%

SCS SHAREHOLDERS ARE SITTING PRETTY

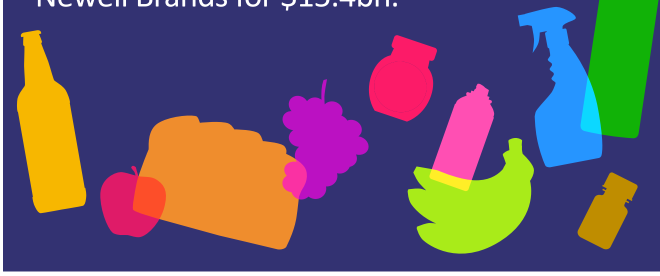
BASED ON 43.2P per share of total cash returns, this is the equivalent percentage return investors have enjoyed from **ScS (SCS)** on its 175p IPO issue price since it re-listed on the stock exchange in January 2015. While the consumer backdrop is becoming tougher for big ticket retailers, the 'Sofa Carpet Specialist', which went into administration in 2008, is proving resilient. Full year results (3 Oct) revealed growth across all areas of the group for the third year in a row, while strong cash generation underpinned a 1.4% total dividend hike to 14.7p. (JC)

CONSUMER PRODUCT EXPERTS RAISE $1.25BN FOR NEW CASH SHELL

A GROUP OF individuals previously at US consumer products group Jarden have raised $1.25bn for the launch of a new buy-and-build business called **J2 Acquisition (JTWO)**.

The cash shell has started trading on London's Main Market and will seek to buy businesses in undisclosed sectors.

J2 has been set up by Jarden's co-founder Martin Franklin alongside other former Jarden executives Ian Ashken and James Lillie. Jarden was acquired last year by Newell Brands for $15.4bn.



US RECESSION? ALMOST NO CHANCE

THERE IS VIRTUALLY no chance of the US economy plunging into recession during the next 12 months, say economic strategists at investment bank UBS.

The analysts input many hard and soft data points into their model and find that a 'US recession probability is still close to zero'.

Hard data is fact based; numbers, statistics and charts, say. It takes me 40 minutes to get to work in the morning, for example. Soft data is subjective and highly variable. I think it is quicker to get the tube to work rather than the bus.

'Although the gap between hard and soft data is large, the implied recession probabilities are actually in sync and show no signs of a slowdown ahead,' says UBS.

That's good news for investors everywhere given the size of the US economy and the ramifications for a slowdown rippling elsewhere. When the US sneezes, everyone catches a cold, as the saying goes.

Market is too gloomy on Vodafone

Growth in Europe and peer-beating dividends on offer

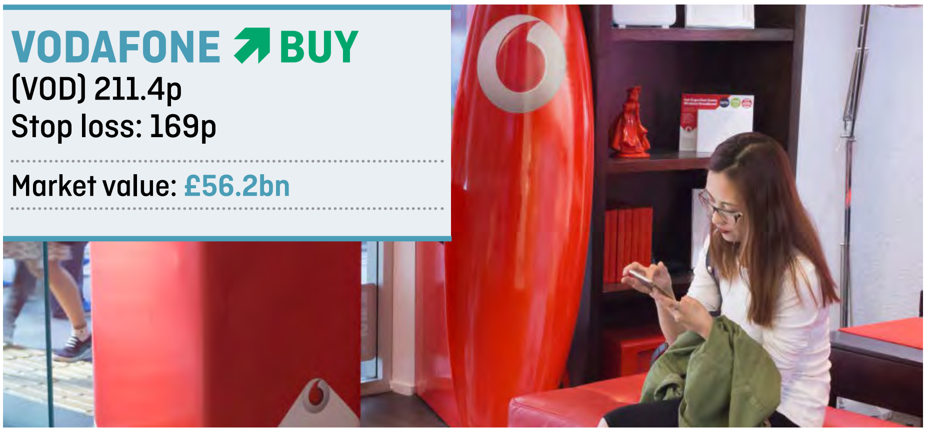
One of the largest communications network providers, **Vodafone (VOD)** supplies more than 523m mobile customers worldwide. The FTSE 100 mega-cap is also a staple portfolio stock for thousands of investors thanks to its substantial dividend.

This year's expected income of around €0.15 per share (the group reports in euros) implies a 6.3% yield, the fifth highest on the FTSE 100.

The dividend looks secure, in our opinion. The market waking up to this fact could result in a share price re-rating towards 280p levels, going by the target price of investment bank UBS.

VODAFONE BUY
(VOD) 211.4p
Stop loss: 169p

Market value: £56.2bn



SHARE PRICE DRAG

The stock has nudged lower because of competition worries and thanks to the strengthening pound versus the euro.

Aggressive promotions are anticipated from Iliad, a new entrant in Italy where Vodafone earns about 12% of its service revenue. We believe the group has the financial muscle and brand strength to bat this threat off over the medium-term. Vodafone faced a similar problem in India in the recent past, but that cut-throat battle is easing off.

RETURNING TO GROWTH

While the market has homed in on these negatives, it seems to be underplaying success elsewhere in Europe, and emerging economies in Africa, the Middle East and Asia Pacific (AMAP). This is thanks to Vodafone's unified communication strategy which combines high-quality voice, data, cloud for business, and entertainment services across a wide range of technologies and screens to both consumers and enterprises.

Various countries are also providing hefty subsidies to encourage broadband deployment. Germany, for example, has earmarked €24bn over the next few years, and Vodafone is one of the best funded and biggest investors.

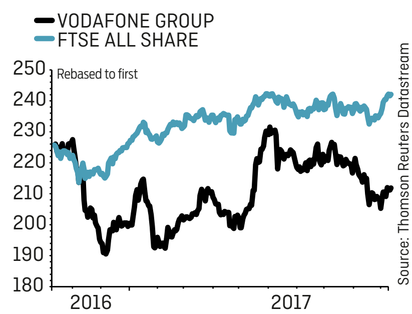
Most analysts anticipate the first real growth from Vodafone in years. Estimates imply mid-single digit pre-tax profit expansion this year to 31 March 2018, and underlying revenue progress. There is also scope for another hefty chunk of costs to be stripped away, with the company eyeing €7bn in savings.

DISCOUNT VALUATION

Net debt of €32bn this year would be balanced by anticipated €72bn net assets. More than €5bn of free cash flow is expected, comfortably covering the €4.1bn dividend bill.

The stock trades on a 7% equity free cash flow yield, according to UBS, and promises a significantly more attractive income yield than either the average for its sector (4.5%) or the FTSE 100, which averages at about 4%. A 280p share price would bring the yield down to 4.8%, roughly in line with peers. (SF)

BROKER SAYS: 18 7 2



Reckitt remains full of vitality

Consumer health and hygiene titan's competitive advantage remains intact

Share price weakness at consumer health and hygiene giant **Reckitt Benckiser (RB.)** presents a not-to-be-missed buying opportunity for seekers of high-quality, defensive stocks.

Short-term issues currently weigh on sentiment towards the *Dettol*, *Durex*, *Gaviscon* and *Cillit Bang* brands owner, yet we're staying positive on Reckitt for its superior innovation skills, globally-derived earnings and dependable cash flow.

READY FOR RECOVERY

Sentiment towards the FTSE 100 manufacturer and distributor of household, toiletry and pharmaceutical products has soured amid downgrades caused by a weaker top-line performance.

Downward earnings revisions largely reflect disruption caused by a June cyber attack which meant orders ready to be shipped could not be sent. Some unwinding of sterling weakness against the US dollar has also impacted estimates, while investors are also nervous about the full financial impact from a humidifier scandal in South Korea, where consumers have boycotted Reckitt's products.

MARMITE MEAD DEAL

Reckitt's transformational £13bn acquisition of US baby formula maker Mead Johnson Nutrition

RECKITT BENCKISER ↗ BUY
(RB.) £70.37
Stop loss: £56.30

Market value: £48.81bn

has also proved divisive. Bears point to headwinds faced in the US and China and Reckitt's lack of experience in infant nutrition; bulls to Reckitt's increased emphasis on higher margin Health & Hygiene categories and enlarged emerging markets exposure.

Those impatient with the pace of sales recovery at Reckitt are also factoring-in competition from local companies in emerging markets and the re-emergence of cheaper private label products, particularly in the US amid the rise of discounters and the online channel.

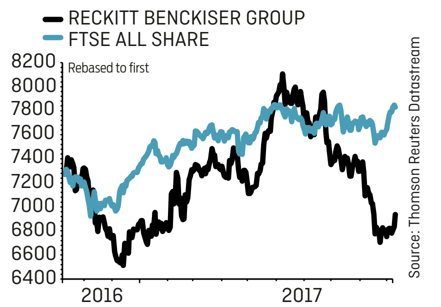
But we're in agreement with Berenberg, which has reiterated (9 Oct) its 'buy' rating and £85 price target, which represents 21% upside from current levels for a business with high margins, excellent cash generation, strong returns on invested capital and a robust balance sheet.

Acknowledging soft recent growth trends, Berenberg doesn't believe Reckitt's competitive advantage in innovation and health has eroded and expects 'the top line to accelerate back to a sector premium', also flagging up the £48.8bn cap's proven ability to 'premiumise a category'.

Shares also welcomes the sale (19 Jul) of Reckitt's food business, including the *French's*, *Frank's RedHot* and *Cattlemen's* brands, to US spices giant McCormick for $4.2bn.

Divestiture proceeds will be used to pay down debt arising from the Mead Johnson takeover, Berenberg forecasting a reduction from a 2017 year-end £9.5bn to £8.1bn in 2018, then £6.66bn by the end of 2019. Even in the face of current headwinds, Berenberg forecasts improved earnings per share of £3.04 (2016: £2.24) and a £1.86 dividend (2016: £1.53) this year, building to £3.54 and £2.16 in 2018 respectively, a testament to Reckitt's diversity and resilience. (JC)

BROKER SAYS: 11 11 2



SDX ENERGY

(SDX:AIM) 52p

Gain to date: 35.9%

Original entry point:

38.23p, 2 February 2017

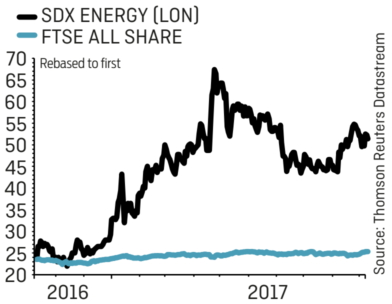
NORTH AFRICAN OIL and gas producer **SDX Energy (SDX:AIM)** is heading in the right direction again after announcing a discovery on its West Garib concession, onshore Egypt.

The Rabul 2 well looks to have identified a larger find than that delivered by the Rabul 1 well drilled in July, with 105.1 feet of net pay.

A reservoir or portion of a reservoir which contains oil or natural gas economic to produce is known as 'pay' as it is literally capable of 'paying' an income. Net pay is what is left after applying further criteria such as how much oil can pass through the rock in the sub-surface.

The remainder of the year is likely to see focus switch to Morocco where the company plans to drill seven wells. Five development wells will be drilled on the already-producing Sebou permit and two exploration wells will be drilled on the Lalla Mimouna permit.

Cantor Fitzgerald analyst Sam Wahab says: 'All locations in the Sebou permit are adjacent to existing infrastructure and therefore we believe the wells can be placed on production quickly in a success case.'



SHARES SAYS:
Cantor has a price target of 84p and we also see scope for material upside. Keep buying. (TS)

BROKER SAYS: 1 0 0

IMPAX ASSET MANAGEMENT

(IPX:AIM) 150.5p

Gain to date: 18.9%

Original entry point:

126.6p, 21 September 2017

OUR BULLISH STANCE on sustainable investment focused asset manager **Impax Asset Management (IPX:AIM)** is paying off. The company's recent acquisition of US peer Pax World Management has clearly sparked renewed interest in Impax.

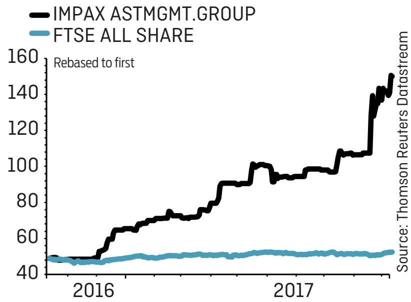
The deal, expected to close by February next year at the latest, will add an extra 42% of assets under management (AUM). This would bring the company's AUM to £10.3bn, and potentially attract more institutional investors to the firm's products.

Investor sentiment towards the asset manager is extremely positive at the moment despite tough regulations such as MiFID II coming in early next year. The company was already enjoying a successful 2017 even before the acquisition news broke.

Back in May, we flagged the company due to the large amount of inflows into its funds.

Stuart Duncan, analyst at Peel Hunt, notes this pattern is continuing as Impax took in £402m in net new money in the three months to 30 September.

Duncan has upgraded his 2017 pre-tax profit and earnings per share forecasts both by 6%, to £8.4m and 5.1p respectively.



SHARES SAYS:
Keep buying the stock as the company is set to benefit from a greater US presence through its Pax deal (DS)

BROKER SAYS: 1 0 0

THIS IS AN **ADVERTISING FEATURE**

A scary fact you can't ignore

Here's what the investment industry won't tell you

A few years ago a smart hedge-fund manager was asked his opinion about a popular investment strategy. He replied:

"To make 5% a year, you're risking half your money. That to me is an awful trade. I don't make it."

Would you risk half your capital to make 5% a year? I doubt it.

So what's the high-risk investment he's referring to? Some fancy derivative? Trading commodities? Putting money in a start-up?

No. He was talking about putting your money in the stock market.

He explained, "Since the year 2000 stocks have had two distinct declines north of 50%. So to make 5% a year you're risking half your money. That's an awful trade."

This isn't what most investors or advisers believe. The accepted view is that stocks beat any other type of investment over the long term. OK, that's true. But those innocent-looking four words - "over the long term" - conceal a real danger.

The fact is many investors don't have a very long time frame. Most of us don't really get started until our forties or even fifties. Before that we had lower salaries and families and mortgages to pay for. So we don't have the luxury of decades of investing. Also the closer you get to retirement age, the less you want to risk your savings.

Let's say you're in your fifties with another fifteen years of working life. Would you be happy if half your money disappeared in a 50% crash? Hardly. A crash coming at the wrong time would have serious consequences for you.

Here's one answer. The gloomy scenarios I've described rely on one popular approach: "passive investing" - putting your money in the market and leaving it there. When a 50% crash happens, your money goes down with the market.

Is this necessary? No. Trend investing – which is the approach we follow at Saltydog Investor – helps you avoid big downturns. It's an active approach to investing.

When the market goes up, you switch your money into the best-performing sectors. And when the market heads down, you move your money into safer assets, or even out of the market entirely.

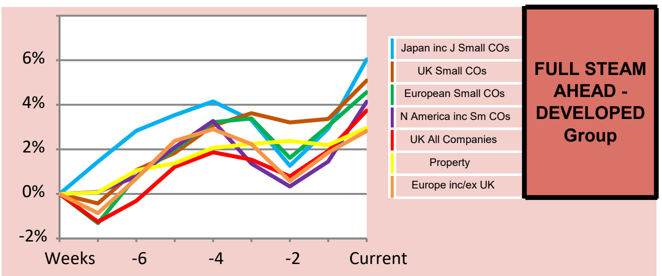
OK, it's not for everyone. But it's perfectly practical and easy to use for anyone who wants to take more control of their investments. Crucially, it means that you don't have to just sit and watch when the market goes into a nosedive. You can actively manage your money, so that you're not risking half of it for 5% a year.

For a full explanation about how our trend investing system could give you better – and less volatile – returns from the stock market, please take a look at our website: www.saltydoginvestor.com

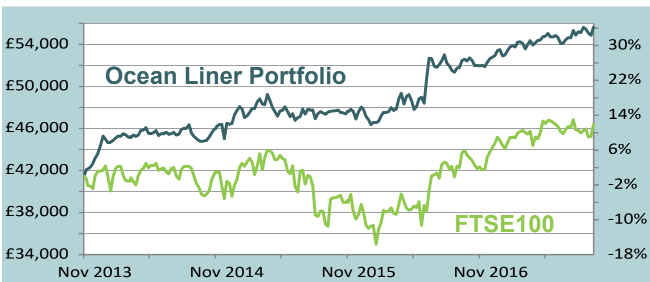
Plus we offer a 2-month free trial, so you can see how well it works for you, at absolutely no cost. Do give us a visit!

Just go to: www.saltydoginvestor.com

Spot new trends, with clear, easy-to-follow charts & data



Follow our market-beating portfolio



FREE TRIAL Try our trend investing system, free for 2 months. Go to: www.saltydoginvestor.com

Why Royal Mail is the ultimate contrarian play

We explain the issues facing the UK parcels and letters delivery group and why the stock is still attractive

The strikes facing parcel delivery service **Royal Mail (RMG)** are just the latest in the series of problems dragging on the company's performance.

Approximately 111,000 postal workers will go on strike between 19 and 21 October over pay and pensions. This is despite Royal Mail already paying staff above-industry rates and generous pension contributions.

The profitability of the company is highly sensitive to small changes in wage inflation assumptions. Concerns over competition and dwindling letter volumes have also weighed on the stock.

Shares in the postal service have taken a beating this year, down 17% to 381p. That's higher than the 330p price at which it joined the stock market in October 2013 but well below the all-time high of 604.5p seen in January 2014.

> SHARES HAVE BEEN WEAK BUT ARE STILL TRADING ABOVE THEIR IPO PRICE

Many analysts are negative on Royal Mail as an investment – yet we believe a large amount of bad news has already been priced in and that now is a good time to buy while sentiment is so poor towards the business.

To its credit, the business continues to become more efficient and flexible and is rapidly increasing its position overseas.

Furthermore, many rivals on the parcel delivery side have developed a poor reputation for service, creating an opportunity for Royal Mail to win back lost customers.

HOW DAMAGING WOULD A STRIKE BE?

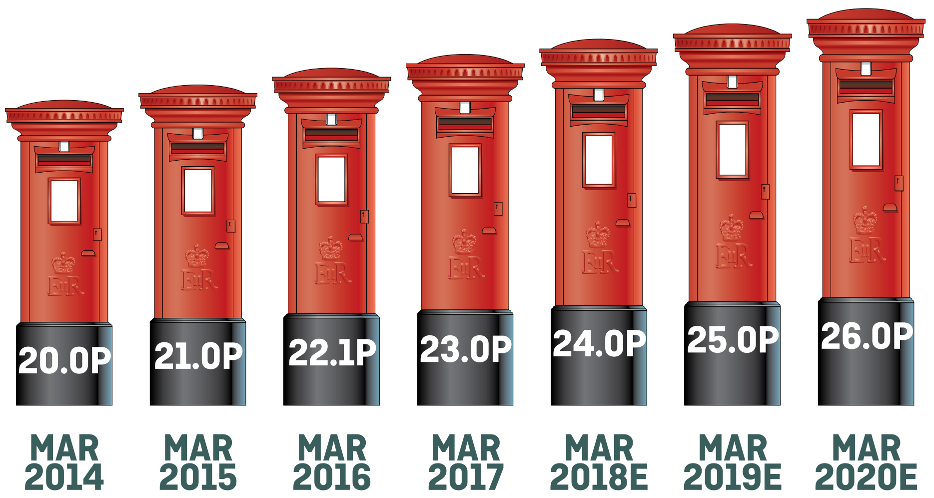
RBC Capital Markets analyst Damian Brewer thinks the forthcoming strikes risk material damage to Royal Mail. He believes competitors might take advantage of the strikes to steal market share 'that might never return'.

WHY ARE POSTIES STRIKING?

Royal Mail wants to replace its defined benefit pension scheme which provides a guaranteed income in retirement with a different scheme that gives employees a cash lump sum linked to the value of their contributions.

Workers are also unhappy with pay, which Royal Mail hopes to address through a

ROYAL MAIL'S DIVIDEND PROFILE



Source: Digital Look, Investec. E=Estimated.

5% increase over two years that is partially dependent on much-needed productivity improvements.

Outside these issues, the company is struggling with 'business uncertainty' in the UK and declining letter volumes as electronic communication such as emails and texts continue to replace 'snail mail'.

UBS analyst Dominic Edridge is pessimistic that Royal Mail can continue to grow due to its lack of modernisation. An example of which is the high pricing for heavier parcels as they have to be manually sorted.

WHERE IS ROYAL MAIL INVESTING MONEY?

The company is working on diversifying its business by focusing on e-commerce, investing in technology and expanding its overseas division, GLS.

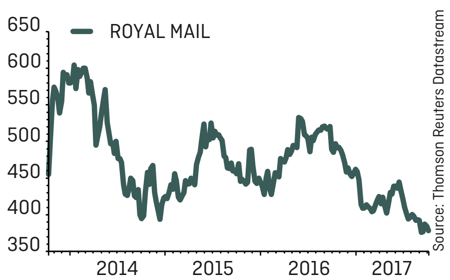
Revenue from GLS increased 18% in the three months to 25 June, with sales growth delivered in all main markets. This is promising although GLS only accounted for circa one fifth of group revenue and profit in the last financial year.

Under its overseas expansion plan, Royal Mail acquired Golden State Overnight in the US last year, which is currently performing in line with expectations.

In April, Royal Mail made further progress with its strategy through the acquisition of US overnight parcel delivery firm Postal Express for $13.3m.

WHY SHOULD INVESTORS STICK WITH ROYAL MAIL?

The stock was a big hit when it floated four years ago as it was priced on a low rating and paid a generous dividend.



Current forecasts imply a prospective yield in the region of 6.3% and the potential for a bit more dividend every year.

In May, the dividend was lifted 4% to 23p per share and Investec analyst Alex Paterson thinks the dividend per share will continue to rise, forecasting 24p in the year to 31 March 2018, increasing to 25p and 26p in 2019 and 2020 respectively.

Despite the troubles clouding Royal Mail's outlook, he remains 'optimistic that significant efficiencies can be achieved over time' but concedes that this may take longer than expected.

Paterson also flags that trading in the three months to 25 June was better than forecast; partially driven by a strong performance overseas.

Liberum analyst Gerald Khoo forecasts EBITA (earnings before interest, tax and amortisation) will grow in the GLS overseas division from £164m to £188m in the year to 31 March 2018.

The group as a whole currently trades on 9.3 times forecast earnings per share for the current financial year. That is far too cheap in our opinion for a company with such a strong market position. Yes, it deserves a discount for labour issues and competitive threats – but not to such a dramatic level.

It is easy for investors and analysts to overlook Royal Mail's qualities given the headwinds it faces. However, we believe its problems can be fixed and investors are being rewarded for their loyalty with a generous yield. (LMJ)

PREPARE FOR RISING INTEREST RATES

WHAT TO DO WITH **YOUR INVESTMENTS**

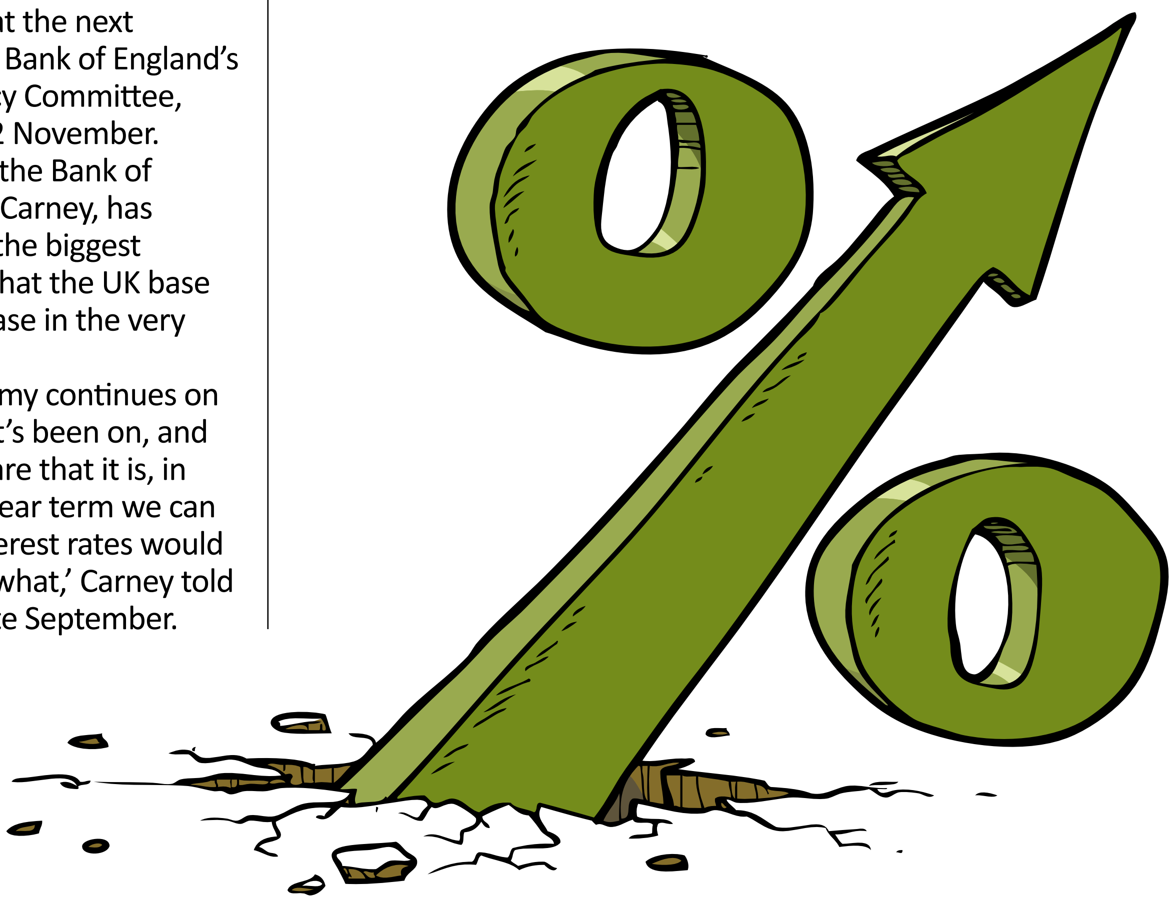
STEVEN FRAZER

UK interest rates have to rise at some point and it seems we are fast approaching that day. Market commentators now believe the first rate increase in a decade could happen at the next meeting of the Bank of England's Monetary Policy Committee, scheduled for 2 November.

Governor of the Bank of England, Mark Carney, has recently given the biggest indication yet that the UK base rates will increase in the very near future.

'If the economy continues on the track that it's been on, and all indications are that it is, in the relatively near term we can expect that interest rates would increase somewhat,' Carney told BBC radio in late September.

His more hawkish comments on a near-term rate increase caught the market by surprise. Most economists were not anticipating a rate rise until well into 2018.



WHAT DOES A RATE RISE MEAN FOR SAVERS?

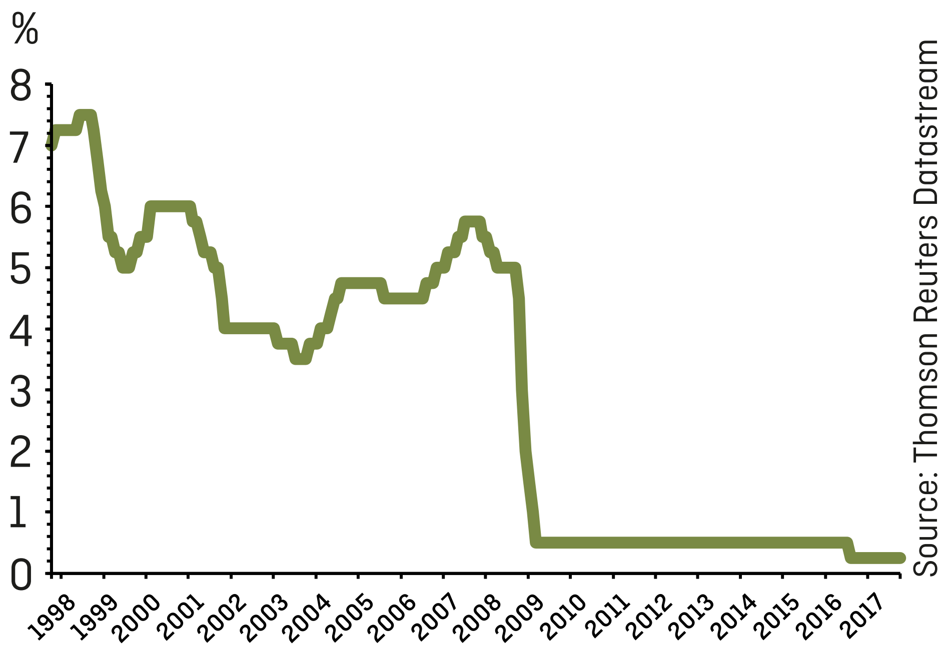
For cash savers, rising interest rates will come as a relief as it holds out the prospect of finally being able to get a better return on cash deposits than seen for many years.

Interest rates have been low and generally less than the rate of inflation since 2008, thus the real value of the money on deposit has been eroded.

Although hiking interest rates should help savers, they still need to be vigilant as savings providers may not increase rates by as much as hoped. We're also unlikely to see interest rates quickly increase by a large amount once they do start to move up.

Research from independent savings advice website Savings Champion shows five years ago, when the base rate was 0.5%, the average easy access account was paying 0.74%. Today that average rate has fallen to 0.35% and the Bank of England's official rate sits at 0.25%.

UK INTEREST RATES OVER LAST 20 YEARS



> MOST ECONOMISTS WERE NOT ANTICIPATING A RATE RISE UNTIL WELL INTO 2018

HOW A 0.25% BASE RATE RISE MIGHT AFFECT CASH SAVINGS

Savings type	Current best buy rate	Best buy after 0.25% rise
Easy access	1.26%	1.51%
Notice account	1.60%	1.85%
Easy access ISA	1.10%	1.35%
Notice ISA	1.30%	1.55%
1 year fixed rate bond	1.95%	2.20%
3 year fixed rate bond	2.20%	2.45%
5 year fixed rate bond	2.45%	2.70%

Source: Savings Champion

IS A RATE RISE GOOD OR BAD FOR INVESTORS?

Many investors presume that rising interest rates are bad news for stock markets yet this is not necessarily the case, according to data provided by trading company Salt Invest.

Its analysts looked at the performance of the FTSE 100 index and the more domestically-orientated FTSE 250 index during the last three periods of rising UK base rates. The results show that both the large and mid-cap indices continued to rise in value or held firm against the backdrop of rising interest rates.

> IN THE PAST, BASE RATE RISES SEEM TO HAVE BEEN GENERALLY POSITIVE FOR THE UK MARKET

STOCK MARKET PERFORMANCE DURING PREVIOUS RATE HIKE PERIODS

Period	Base rate rise	FTSE 100 change	FTSE 250 change
May 1988 – October 1989	7.5% to 15%	20.1%	12.9%
May 1999 – February 2000	5.25% to 6%	0.01%	14.4%
October 2003 – July 2007	3.5% to 5.75%	48.4%	98.1%

Source: Salt Invest

'Escalating base rates may mean that interest paid on deposit accounts increases and so the returns on quoted companies may become increasingly less attractive,' says Salt. That latter comment looks a bit extreme when you consider that interest rates aren't expected to jump back to the 5%+ territory to which many of us were accustomed a decade ago.

Theoretically better rates on lower risk assets, such as long-term savings products, eat into the relative attractiveness of higher risk equities. However, we cannot see a scenario in the near future where cash will provide a better return than the 5-6% you've historically been able make from the stock market each year. As such, we don't believe investors will rush to dump their stocks as soon as rates rise.

Nonetheless, we do believe that investors will rejig their portfolios as there are obvious winners and losers from rising interest rates. We'll discuss some of the sectors like banking and housebuilding later in this article.

'In the past, base rate rises seem to have been generally positive for the UK market,' admit analysts at Salt. 'Inflation normally goes up when the demand for goods and services rises more rapidly than an economy's productive capacity.

'Base rates are applied as a brake to allow for measured and sustainable economic growth; something that's illustrated by the performance of many stocks.'

A glance across the pond is worthwhile. US interest rates started rising in December 2015, the first hike in almost 10 years.

'Despite a number of rate rises in the US, it hasn't stopped the Dow Jones Industrial Average climbing 28% over the same period,' the investment experts point out, 'or the S&P 500 rallying 25% to current record highs of around 2,545.'

WHAT ABOUT BONDS?

Changes in interest rates will affect the value of bonds in your portfolio. If rates are rising, newly issued bonds with higher rates on the market will be more appealing than older bonds in your portfolio paying less. This situation can reduce demand for your existing bonds and push down their resale value.

When rates are rising, short duration bonds could be more appealing than ones with longer maturities as the latter tend to suffer most because they lock investors into lower rates for extended periods.

WHAT ABOUT YOUR OWN PERSONAL FINANCES?

Rising repayments on your home is a big consideration if you have a tracker mortgage. Repaying a mortgage is the biggest monthly outgoing for many people.

While the mooted move from a 0.25% base rate to 0.5% is unlikely to put a big squeeze on monthly household budgets, a sustained rising trend could have an impact.

Three or four rate rises over the next couple of years – which is not out of the question – would likely mean substantial household belt-tightening.

According to the Bank of England, 43% of homeowners are on variable or tracker rates.

On the average mortgage of £125,000, an increase of 0.25% would increase monthly payments by £15 to £665. That would amount to an extra £185 per year, according to Nationwide's data.

But while the impact of the first hike may be small, someone with a mortgage of £150,000 could find themselves paying an additional £161 a month if rates increased by 2%, according to figures supplied by the Halifax, Britain's largest lender.

Companies will also face the same test with regards to corporate debt repayments.

RISING RATES COULD HIKE MORTGAGE REPAYMENTS

Average monthly repayment	% rise in mortgage rate	Increase in monthly repayment
£679.74 (current average for new mortgages)		
£698.90	0.25%	£19.15
£718.36	0.50%	£38.61
£738.13	0.75%	£58.38
£758.20	1.00%	£78.48
£778.56	1.25%	£98.82
£799.23	1.50%	£119.48
£820.18	1.75%	£140.44
£841.43	2.00%	£161.69

Based on £150,000 mortgage loan
Source: Halifax

WHAT DOES THE CURRENT ECONOMIC DATA SUGGEST?

Alan Haldane, the Bank of England's chief economist, has been at pains to highlight the positives of a rate rise.

Such an event would be a sign of the economy healing, and therefore adjusting to that healing process. 'So rather than being a source of fear or trepidation, this ought to be a good news story about the economy proving resilient,' he recently told *Sky News*.

Although the Bank of England has highlighted 'pockets of risk' among consumer debt, macro data seems supportive of rate rises, not least the inflation figure which is currently above the Bank of England's 2% target.

'Inflation and unemployment figures might suggest a rate rise in merited, but flaccid wage growth does not,' says Russ Mould, investment director at investment platform AJ Bell.

'Wage increases continue to run below inflation and this apparent break down in the Phillips Curve, which asserts low unemployment should lead to higher wage increases (and vice-versa), does still seem to be a major factor in Bank of England thinking,' he adds.

EXPERT OPINIONS ARE SPLIT

Samuel Tombs at Pantheon Macroeconomics says the UK services sector remains 'stuck in a rut,' casting doubt over whether the Monetary Policy Committee will press ahead with a rate rise over the coming months.

'The latest PMIs (purchasing

10 YEAR COMPARISON

	Jul-07	Now*
Bank of England base rate	5.75%	0.25%
Unemployment rate	5.3%	4.3%
CPI inflation	4.4%	2.9%
Wage growth	4.5%	2.1%
Real wage growth	0.1%	(0.8%)
House price inflation	10.6%	5.1%

Source: Thomson Reuters Datastream, ONS, Bank of England, AJ Bell
*Latest reported figures as of 10 October 2017

managers' index data) – especially the decline in their forward-looking balances – do not warrant such optimism,' he adds.

Economic experts at Russell Investments go further, claiming an interest rate rise this year against a backdrop of weak underlying growth would be 'a mistake'.

'If the Bank of England chooses to hike rates this year, we expect the underlying growth slowdown to take centre stage again, especially when inflation starts to roll over,' says Russell's senior investment strategist Wouter Sturkenboom.

A cooling in the housing market, mixed industrial sentiment surveys and the debate over what Brexit may or may not mean for the UK's economic prospects are additional complications.

STOCKS:

POSSIBLE RATE RISE WINNERS

Rising interest rates are considered to be positive for the domestic currency so you could assume that sterling will strengthen near-term.

In general, the higher rates that can be earned tend to attract foreign investment, increasing demand for the home country's currency.

Such a situation implies a negative outlook for the FTSE 100 which has a high proportion of overseas earners. They benefit from weak sterling as they get a translational benefit when reporting foreign earnings in sterling. So a strong sterling has the opposite effect and could trigger analysts to downgrade earnings forecasts.

The biggest beneficiaries from rising UK base rates are likely to be the big importers and the UK-dominant banks. It should be good news for retailers which source a lot of products from overseas, although they face the risk that consumers have less spare cash to spend in the shops if their credit card, loan and mortgage repayments are pushed up.

Retailers which buy goods from overseas include **Next (NXT)** and Primark-owner **Associated British Foods (ABF)**. The cost of products, in sterling terms, will be reduced which should allow for higher margins and increased earnings.

We're more cautious on over-spaced, structurally-challenged shopkeepers. Operators such as **Debenhams (DEB)** are best avoided from an investment perspective, in our view, while near-term prospects suggest investors should steer clear of **Dixons Carphone (DC.)** and **DFS (DFS)**.

They sell higher-ticket items like mobile phones, laptops and sofas whose purchase could easily be delayed by consumers under financial pressure from higher cost of servicing debts.

WHICH BANKS LOOK GOOD?

Banks and other financial stocks tend to enjoy fatter profit margins in rising interest rate environments which also serve to provide a lift to earnings and ultimately their share price.

In theory, that should play well for all of the major high street lenders including **Barclays (BARC)**, **HSBC (HSBA)**, **Lloyds (LLOY)**, **Royal Bank of Scotland (RBS)**, along with smaller challenger banks. These include **Aldermore (ALD)**, **Metro Bank (MTRO)**, **OneSavings Bank (OSB)** and **Virgin Money (VM.)**.

Rising base rates will allow the banks to charge borrowers higher rates while probably only

paying a little more to savers.

At the moment we're big fans of Virgin Money as an investment as its shares trade on a low valuation and it has considerable growth prospects. We believe it is capable of stealing a much larger market share than its current 3% or so of the UK mortgage market.

We're more cautious on Lloyds following the recent acquisition of credit card company MBNA. In our view, this increases its exposure to unsecured lending which raises the risk that the bank's capital buffers could be damaged if there is an economic downturn.

STOCKS:

POSSIBLE RATE RISE LOSERS

A rising interest rate is bad for companies with high debt levels, particularly those which have to refinance their debts in the near future as they could incur higher repayment costs.

Consumer-related property companies also look vulnerable, in our view. Rising mortgage rates (off the back of rising interest rates) could make it harder for some people to get on the property ladder, thus sentiment could wane towards housebuilders, in particular.

Since the Brexit vote, shares of housebuilders like **Barratt Developments (BDEV)**, **Berkeley Group (BKG)**, **Bovis Homes (BVS)**, **Persimmon (PSON)** and **Taylor Wimpey (TW.)** have enjoyed a good run. Now could be a good time to reduce exposure to the sector.

'The housebuilders are sitting ducks, as the housing market is in for a shock when rates finally begin to rise again,' say

HOUSE PRICES VS MORTGAGE DEBT

Quarterly data. Source: Bank of England, Halifax, Berenberg calculations. Data are indexed: 100 = Q1 2007.

Salt's market experts. 'It does look as though the current year will see earnings peak for the housebuilders, as they get hit by the double whammy of house price inflation cooling off and building costs rising.'

At the moment we like **MJ Gleeson (GLE)** in the housebuilding space as its premium valuation is justified by exposure to a resilient affordable housing niche in the north of England. We also favour **Telford Homes (TEF:AIM)** whose focus on relatively affordable homes in London should protect its own growth prospects.

A strong run for larger housebuilder Berkeley has left it looking particularly vulnerable to any slowdown in its high end London market. (SF)

WEEK AHEAD

FRIDAY 13 OCTOBER	
TRADING STATEMENTS	
ASHMORE	ASHM
MAN	EMG
PROVIDENT FINANCIAL	PFG

MONDAY 16 OCTOBER	
TRADING STATEMENTS	
POLYPIPE	PLP
RIO TINTO	RIO
SCHRODERS	SDR
AGMS	
AXIS BANK	AXB
BLUEJAY MINING	JAY
ZIBAO METALS RECYCLING	ZBO
ECONOMICS	
UK	
RIGHTMOVE HPI	

TUESDAY 17 OCTOBER	
FINALS	
ASOS	ASC
BIOVENTIX	BVXO
BELLWAY	BWY
DOTDIGITAL	DOTD
ORCHARD FUNDING	ORCH
UTILITYWISE	UTW
INTERIMS	
BP MARSH & PARTNERS	BPM
TRADING STATEMENTS	
BHP BILLITON	BLT
EVRAZ	EVR
MEDICLINIC INTERNATIONAL	MDC
MERLIN ENTERTAINMENTS	MERL
MONEYSUPERMARKET.COM	MONY
PEARSON	PSON
SEGRO	SGRO
VIRGIN MONEY	VM.
ECONOMICS	
UK	
CPI	
HPI	
RPI	
PPI	

WEDNESDAY 18 OCTOBER	
FINALS	
SOFTCAT	SCT
INTERIMS	
U AND I	UAI
TRADING STATEMENTS	
HOCHSCHILD MINING	HOC
RATHBONE BROTHERS	RAT
RECKITT BENCKISER	RB.
AGMS	
BHP BILLITON	BLT
INDIA CAPITAL GROWTH FUND	IGC

THURSDAY 19 OCTOBER		
FINALS		
TRISTEL	TSTL	
INTERIMS		
STOBART	STOB	
UNILEVER	ULVR	
TRADING STATEMENTS		
GENEL ENERGY	GENL	
RANK	RNK	
RENTOKIL	RTO	
SEGRO	SGRO	
TRAVIS PERKINS	TPK	
UNILEVER	ULVR	
ECONOMICS		
UK		
RETAIL SALES		
EX-DIVIDEND		
ACTION HOTELS	AHCG	0.77P
AMATI VCT	AT2	3.25P
BAE SYSTEMS	BA.	8.8P
BURFORD CAPITAL	BUR	$0.03
CAPITA	CPI	11.1P
CITY OF LONDON INVESTMENT TRUST	CTY	4.3P
HARVEY NASH	HVN	1.64P
HOWDEN JOINERY	HWDN	3.6P
MEARS GROUP	MER	3.45P
JOHN MENZIES	MNZS	6P
MP EVANS	MPE	5P
MARSHALLS	MSLH	3.4P
NEWRIVER RETAIL	NRR	5.25P
SMITHS GROUP	SMIN	29.7P
SMART METERING SYSTEMS	SMS	1.74P
SENIOR	SNR	2.05P
STILO INTERNATIONAL	STL	0.05P
S & U	SUD	28P
WILMINGTON	WIL	4.6P

Click here for complete diary
www.sharesmagazine.co.uk/market-diary

EXPECT STRONG FULL year results from digital marketing technology supplier **DotDigital (DOTD:AIM)**. This will likely mean impressive near-20% organic top line growth, implying £32m revenue or so.

Pre-tax profit should be in the £8m ballpark and be backed up by excellent cash generation. A June 2018 price to earnings multiple nudging 27 remains the sole factor to give prospective investors pause. (SF)

LOOK FOR AN update on the sale process for its spreads business when consumer goods giant **Unilever (ULVR)** reports third quarter results on 19 October.

The company hopes to net $8bn from a sale of the business which makes Flora and Stork margarines.

The market will also be looking for a progress report on the wider 'Connected 4 Growth' programme and review launched in the wake of a rebuffed $143bn bid from Kraft Heinz earlier this year.

ENERGY BROKER UTILITYWISE (UTW:AIM) releases its full year results on 17 October. The company's share price has been weak lately which suggests the market is still expecting more bad news.

We note that Panmure Gordon analyst Michael Donnelly in August raised his rating on the stock to 'buy' for the first time in more than two years. He had correctly spotted the company's aggressive accounting techniques which ultimately contributed to a large reduction in the value of the shares.

Donnelly says a potentially valuable business may now emerge 'as the fog of overstated earnings begins to clear'.

Concentrated equally weighted portfolios

ADVERTORIAL

GUINNESS
ASSET MANAGEMENT LTD

Matthew Page co manager of Guinness Asset Management's Global Equity Income Fund and Global Innovators Fund, explains his rationale for using concentrated equally weighted portfolios in these funds

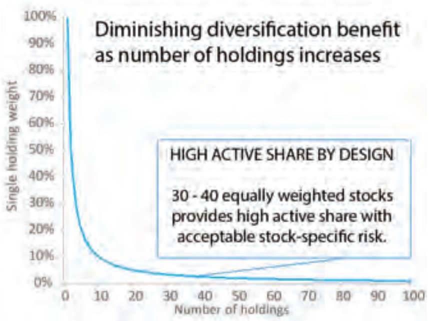
With 35 positions each kept at around 2.8% of the fund, our typical fund portfolio structure is both concentrated and elegant in its simplicity. Elegance, however, is not our main objective; what matters to us is the effect of this structure on portfolio risk and how it can help us make good returns.

WHY CONCENTRATED?

As active managers, we only want to own the best shares, and few enough of them that each can contribute meaningfully to performance.

HOW CONCENTRATED?

History shows that unexpected company disasters can happen despite the most thorough due diligence. With multiple holdings, a portfolio's maximum loss is the size of the largest holding. Given the types of company we are investing in, we are comfortable with positions of 2.5-3.3% - the loss of which would be by no means disastrous.



WHY EQUALLY WEIGHTED?

Equal weighting allows us to optimise the level of concentration and stock-specific risk efficiently and intelligently. It means that with as few as 30 holdings, a portfolio can have a maximum stock-specific risk of only 3.3%. On the other hand, beyond 40, with each holding at 2.5%, the reduction in risk from adding more is relatively small, and diminishing. The time required for due diligence and monitoring, of course, increases linearly. The sweet spot, therefore, is between 30 and 40.

CONVICTION IN EVERY STOCK

It's worth thinking from first principles about why we keep stocks at equal weights, rather than having favourite stocks – and less-than-favourites.

1. *Can we identify companies that will provide a positive return?*
   Yes, we think we can, by relying on our disciplined investment process.

2. *How confident are we in the scale of this return?*
   Not very. We are cautious with upside predictions, because there are so many variables – not to mention exogenous shocks, which are impossible to predict.

3. *Can you predict the timeframe over which this return will be realised?*
   No. We don't think we – or anyone – can do this reliably.

Given these answers, we believe strongly that an equally weighted portfolio works to our strengths. We think we can identify companies that are undervalued and will provide a positive return, we don't know exactly how much, we know some will lose us money, and we don't know the timeframe.

So, let every good idea have an equal weight, and the market will decide when a more reasonable valuation will be reached.

OTHER BENEFITS OF EQUAL WEIGHT PORTFOLIOS

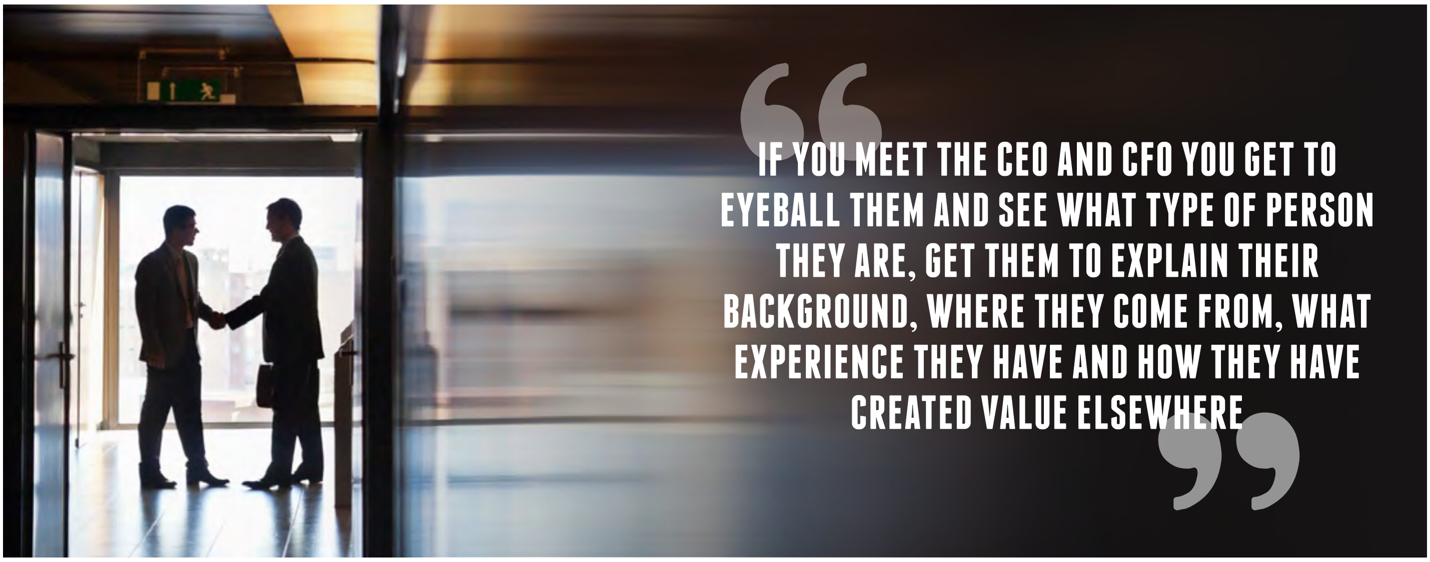
- Rebalancing adds a natural element of 'buy low, sell high' and counters loss aversion
- One in, one out: fixed number of positions keeps the portfolio up to date with current best ideas
- One in one out provides a useful sell discipline; fund managers are better at buying than selling.
- High active share by design: weights are not determined according to the index

Find out more about our distinctive investment process at **www.guinnessfunds.com**

GUINNESS
ASSET MANAGEMENT LTD

Should fund managers always meet investee companies?

Or can investment selections be made purely by analysing spreadsheets?



For 'bottom-up' stock pickers, face-to-face meetings with company management can be the key to obtaining a competitive investment edge. Other professional fund managers, however, prefer to pore over annual reports and undertake forensic analysis of the profit and loss account and balance sheet. By investing purely on the fundamentals, they seek to avoid allowing management teams led by skilled presenters to skew their investment thinking.

KISSING FROGS APLENTY

Wearing out the shoe leather to visit management on-site, or setting aside time to host executives in-house, is part and parcel of most professional money managers' jobs.

'We kiss a lot of frogs,' says Ben Rogoff, manager of the **Polar Capital Technology Trust (PCT)**, who says his investment team meets more than 1,000 companies every year. Fraser Elms of Herald Investment Management is even busier, saying the Herald team (which includes star fund manager Katie Potts) talks face-to-face with 1,500 companies a year, on average.

James Milne of Crux Asset Management, the group behind the **FP CRUX European (GB00BYQJX435)** and **FP CRUX European Special Situations (GB00BTJRPW12)** funds, is also a fan of meetings. He comments: 'Because the annual report is read by competitors, suppliers and customers, management are wary of revealing too much to investors because they are aware other people are reading it as well. When you meet the management, they can help you complete the story. Often company statements don't explain in plain English the background of the company and what it is trying to achieve.'

Milne adds: 'If you meet the CEO and CFO you get to eyeball them and see what type of person they are, get them to explain their background, where they come from, what experience they have and how they have created value elsewhere.'

He explains that by meeting management teams from several companies in the same sector you can also get a feel for the industry background. 'It's good to check from the horse's mouth if analysts are correct in their growth assumptions and to get an insight into where the company is going to be investing its cash.

'I know some people in my peer group say you can never trust management, that they lie. Management are always going to be positive on their stock but I would struggle to think of an example where management have lied.'

Mark Slater, the star manager behind the **Slater Growth Fund (GB00B0706C66)**, likes to meet management teams ideally at the end of the selection process. 'The rationale is that we prefer to know a lot about a business when we meet management so that we can focus on the questions we want answered. The risk in meeting earlier in the process is that you can end up giving undue weight to what management says about near term trading and lose sight of the big picture regarding the long term prospects of the business.'

WORKING CLOSELY

When it comes to micro-caps, often led by founder CEOs, meeting management is an essential part of the due diligence process for **Downing Strategic Micro-Cap Investment Trust (DSM)**. Seeking to generate long term capital growth through a concentrated portfolio, Downing prefers to take an influential, strategic position in each micro-cap of between 3% and 25%.

Interestingly, Downing's Public Equity team applies a private equity style approach to investing, visiting potential investee companies, proactively engaging and working alongside aligned management teams to drive returns.

> OUR APPROACH TO INVESTING IS FUNDAMENTAL. WE ARE STOCK PICKERS. WE LOOK AT MANY OF THE SAME THINGS AS OTHER FUNDAMENTAL INVESTORS, BUT WE THINK WE DO IT IN A SLIGHTLY DIFFERENT WAY

One indefatigable fund manager who puts in the hard yards is Charles Jillings, director and chief executive of ICM, the manager of **Utilico Emerging Markets (UEM)**, an investor in cash generative infrastructure and utility assets. These span ports, toll roads and airports to power, water and waste and communications assets in developing markets ranging from China and Brazil to Chile, Mexico, Malaysia and the Philippines. 'We're bottom-up investors and we're looking for outstanding value,' explains Jillings, whose fund currently trades at an 11.7% discount to net asset value that could interest growth and income seekers.

Crucially, ICM's dedicated team of analysts visit every single one of UEM's investments, regularly fanning out to Asia, Latin America, Eastern Europe and the Middle East in their quest for companies and sectors displaying the characteristics of essential services or monopolies with a unique product or market position.

Seeking companies with compelling long-term business models that also operate in dynamic economies undergoing urbanisation and with a growing middle class, Jillings says the third piece is management. 'A company can be growing its top line, but if management can't control the cost base, you'll find margins erode and shareholder value is undermined.'

He continues: 'We're driven by the need to see the asset and understand the management. If it is a port, we want to see the port even if it means a day's journey or two. We gain access to management because people see that if we're persuaded, we'll make an investment. If we can't get comfortable with management, if we have to second guess, we'd rather be out.'

KEEP YOUR DISTANCE

Jeremy Lang, partner and co-founder of Ardevora Asset Management, has a very different approach. 'Our approach to investing is fundamental. We are stock pickers. We look at many of the same things as other fundamental investors, but we think we do it in a slightly different way. Like most investors we aim to invest in well managed, low risk businesses. But, unlike most, we think the best way to do this is to take the results of academic research from cognitive psychology, on errors and biases, and apply them to financial markets.'

Ardevora believes successful stock picking requires an understanding of how company managers, financial analysts and investors interact. 'Each group is potentially subject to bias, and the biases affecting each group are different,' continues Lang.

'Cognitive psychology tells us that company managers, despite being intelligent and well informed, are especially susceptible to over-confidence bias. We take the view that, all things being equal, management are likely to push a business harder than is sensible. This is driven by their self-belief, their shareholders' desire for growth and their companies' remuneration policies.'

> COGNITIVE PSYCHOLOGY TELLS US THAT COMPANY MANAGERS, DESPITE BEING INTELLIGENT AND WELL INFORMED, ARE ESPECIALLY SUSCEPTIBLE TO OVER-CONFIDENCE BIAS

THE IMPORTANT FACTORS

To get a sense of whether a company is being run in a sensible way, Ardevora examines how fast the company is growing, how much cash is being generated and what management says about their business and current industry conditions. This all helps Ardevora make a judgement on management's attitude to risk.

'If we think a company is straining too hard for growth or in denial about how difficult conditions are becoming we will not buy the stock. Instead of meeting with management, we prefer to keep a safe distance, judging them instead by observable facts.'

Once Ardevora has identified those well managed companies, it applies the same lessons from cognitive psychology to financial analysts and investors to find mispriced stocks. 'In our view, financial analysts can often under-appreciate how fast, and for how long, unusual businesses can grow, especially relative to superficially similar businesses. By exploiting this tendency we hope to identify interesting growth stocks.'

Lang also says that separately, investors can often become sceptical and nervous about companies after a traumatic event. By exploiting this tendency, Ardevora hopes to identify interesting value stocks. 'When we have identified a group of companies which we believe are being well managed, and there is something interesting going on in the way financial analysts or investors are viewing these companies, we aim to construct a well balanced portfolio which allows our focus on stocks to add value. All stocks are equally weighted. As with our children, we believe it is better not to have favourites.'

FORENSIC ANALYSIS

Lending her view is Samantha Gleave, co-manager on a number of Liontrust funds including **Liontrust European Growth (GB00B7T92B14)**. 'Quite often company managers provide forecasts of future profitability and these can be unreliable and, at times, misleading,' Gleave explains. 'Rather than meet with company management, our investment process is instead based on forensic analysis of companies' financial statements.'

Liontrust's analysis suggests this is a superior approach because of the difficulty company managers and investors have in forecasting the road ahead. 'We think investors often place too much emphasis on the ability of individuals to make forecasts despite a wide body of academic literature that affirms none of us are very good at it,' says Gleave.

'Investors' focus on these profit forecasts results in the mispricing of shares and provides us with a consistent opportunity to add alpha. In our opinion, historical analysis of company cash flows is a far more reliable guide to future profitability and stock price valuation in the medium term. We believe that companies run by conservative managers focused on, and delivering, cash flow will perform significantly better than companies run by aggressive company managers making large cash investments today in order to chase forecast future earnings growth.' (JC)

Using funds to pay your monthly bills

We get recommendations from the experts on funds which pay dividends 12 times a year

Unless you're retired, most of us are used to getting a monthly pay packet with cash paid into our current account which is then used to pay all our regular bills.

Once you're in retirement, the loss of this income stream can be frustrating to some. One solution is to put some of your savings in investment funds which pay dividends once a month, as a source of money to help pay the bills.

These funds don't all pay exactly the same amount of money each month and dividends are never guaranteed payments.

Some funds strive to make equal payments throughout the year and hold back some income so they've got a buffer if times get harder. This is calling smoothing. More cash may therefore be paid out towards the end of the year if the fund does not face any shortfalls and there is excess money in its dividend pot.

EXPERTS GIVE THEIR BEST FUND IDEAS

Chase de Vere's head of communications Patrick Connolly suggests investors should look at **Fidelity Extra Income (GB00B41M2W81)**, which is managed by a strong team led by Ian Spreadbury.

'It typically invests 60% in investment-grade bonds and 40% in high yield bonds, has an excellent long-term record and pays a competitive yield, which is currently 3.7%,' says Connolly. He also flags **Threadneedle UK Monthly Income (GB00B8BV4509)** for its 'consistent record'. The fund is targeted at investors who value a higher and more regular income with a 4.3% yield.

Henderson Fixed Interest Monthly Income (GB00B7GSYN71) is another one for investors to consider, according to Square Mile research manager John Monaghan.

The managers of the fund, Jenna Barnard, John Pattullo and Nicholas Ware, target an income yield of around 6%, although Monaghan says this is not guaranteed and varies due to market conditions.

He adds the smoothed payments from the fund are useful for people looking to 'match income payments with cash outgoings' such as bills.

Charles Stanley pensions and investments analyst Rob Morgan believes funds investing in government bonds should offer a more predictable income stream compared to those investing in equities.

A SELECTION OF FUNDS THAT PAY DIVIDENDS EVERY MONTH
Fidelity Extra Income
Threadneedle UK Monthly Income
Henderson Fixed Interest Monthly Income
Artemis Monthly Distribution
Invesco Perpetual Global Targeted Income
M&G Episode Income
Standard Life UK Real Estate
Threadneedle Sterling Short Dated Corporate Bond Fund

> THE LEAST DIVERSIFIED FUNDS TEND TO BE THE MOST UNRELIABLE, OFTEN DEPENDING FOR INCOME ON A SPECIFIC GEOGRAPHY OR SECTOR OF THE MARKET

WHAT IS IMPORTANT TO CONSIDER WITH MONTHLY DIVIDEND FUNDS?

The managing director of Whitechurch Securities, Gavin Haynes says it is more important to find out where the underlying fund is invested and whether it fits your risk profile rather than get hung up on the frequency of dividend payments.

There is a danger the investment process of a monthly dividend paying fund will be driven by targeting assets which pay out income at certain points in the year rather than those which are of the highest quality.

Haynes recommends that investors spread the risk by investing in a portfolio of funds that are diversified across different assets classes. He highlights **Artemis Monthly Distribution (GB00B6TK3R06)**, **Invesco Perpetual Global Targeted Income (GB00BZB27M05)** and **M&G Episode Income (GB00B7FSJ224)**, citing strong management and well-balanced portfolios.

> IT IS MORE IMPORTANT TO FIND OUT WHERE THE UNDERLYING FUND IS INVESTED AND WHETHER IT FITS YOUR RISK PROFILE RATHER THAN GET HUNG UP ON THE FREQUENCY OF DIVIDEND PAYMENTS

LACKING DIVERSIFICATION

Hargreave Hale investment manager Ian Kavanagh warns the least diversified funds tend to be the most unreliable, often depending for income on a specific geography or sector of the market.

If a sector hits a rough patch, dividends may be cut and there will not be alternative assets in the portfolio to make up the difference. As a result, the income from the fund could fall. He flags **Standard Life UK Real Estate (GB00BJZ2V336)** as a monthly dividend payer that lacks diversification.

Kavanagh is also cautious about investing in Japanese or emerging markets for a reliable income as few have Western style progressive dividend policies. This implies the dividend is not a priority if balance sheets come under pressure.

Among the investment manager's favourites is **Threadneedle Sterling Short Dated Corporate Bond Fund (GB00B7SH5738)** although it has a modest yield of 1.7%.

Morgan says investors should be wary of funds that use 'unconventional means' to enhance their income by using derivatives.

While these financial instruments can boost income, it arguably also adds an extra layer of risk to your investment.

Funds are a great source of income for investors, but you should always look under the bonnet to ensure the underlying investments can deliver the consistency of income payments to meet their current and future needs and that the investments are a suitable fit for your risk appetite. (LMJ)

EUROPE IN 2017: 'THE' INVESTMENT

EUROPE BECOMES THE FLAVOUR DU JOUR

As global economies emerged from a searing financial crisis at the turn of the decade the US and UK seemed to pull ahead of their European cousins. Earnings there lagged; growth tinkered on the edge of deflation; its misaligned cadre of politicians toiled with Grexit and Brexit and much in between.

2017 has switched fortunes – Europe has become the poster-child for its cousins and the catch-up trade. GDP growth is strong. Margins are improving. It has the biggest earnings upgrades in developed markets. Where the US and UK have become victim to populism, Europe has rejected it.

Indeed the strength has not gone unnoticed by the European Central Bank (ECB) with its president Mario Draghi beginning to the prepare the market for a withdrawal of their unprecedented quantitative easing (QE) program, most likely in the latter part of 2018.

The euro has also strengthened, which is now at levels last seen before European QE started in spring 2015. It has meant larger European companies, whose earnings tend to be harvested from across the globe leaving them at the behest of currency swings, have performed less well in recent months. Smaller companies, where we are invested, tend to have more of a domestic focus and so have performed better.

SMALL IS MIGHTY

TR European Growth Trust is a truly small company trust, with a large slice of the portfolio – over 50% - invested in firms under a £1bn market capitalisation. As investors in larger companies in Europe have struggled to find value amid renewed enthusiasm for European shares, they've reset their sights further down the scale and targeted mid-sized businesses, which in-turn have become more expensive. It means the smaller end of the market is one of the last remaining places to find relative value, and it's an area that we have a long history of seeking exciting growth opportunities for our investors.

We're cognizant of the risks that come with investing in much smaller firms: they are more susceptible to market swings than bigger businesses and can be difficult to trade in large amounts, but to offset this and diversify the risk we run a longer stock list than most funds, at around 140 holdings.

WHAT TO BUY

So how do we find the sorts of investments that have the potential for strong capital growth?

We look for businesses with management teams that will continue to take the right decisions to either fix what is broken internally or continue growing their earnings strongly, regardless of geopolitical uncertainties or potential adverse market reactions to more hawkish central banks. It broadly translates into three areas of investment.

'Value' is one – companies that we believe the market is pricing below their intrinsic value. The next is growth-at-the-right-price (GARP): firms whose earnings are perceived to be growing more vigorously than their peers or the wider market, but the trajectory of which is being undervalued by the market. The final is turnaround stories, or 'self-help' as we call it – businesses that have been underperforming and are unloved by the market but striving to change their destinies. Below are some portfolio examples.

Self-help

Van Lanschot - Dutch banking

Van Lanschot is the oldest independent bank in the Netherlands, dating back to 1737. It's in the business of private banking, asset management and merchant banking, and in the process of running off a loan portfolio serving corporate clients.

Back in April 2016 it presented a new strategy designed to reinvigorate the private banking arm – at the time the division earned around half of VL's revenues yet accounted for only 7% of total profits, indicating poor efficiency and enormous scope for self-improvement. Looking forward, it is attempting to be more asset-light and build up its capital ratios, returning cash to shareholders wherever possible. As it stands, its return on equity – a measure of profitability – is poor at around 7%; this we believe should be much higher.

Value

Alma Media

The Trust has taken a number of positions in Finland as we are finding undervalued businesses there which we think will perform well amid an improving economy.

Alma Media purports as a media owner of regional, local and free circulation newspapers for print and online, and the market is pricing it as such. But it should be focusing on what the business is really about: online classifieds - websites that deal in used cars, used equipment and in real estate – of which Alma Media is a market leader. Axel Springer, a similar outfit in Norway, provides guidance in this respect, with the market placing significantly more value on its operations. In our opinion other investors will catch-up with this thinking.

Growth (at the right price)

Zur Rose

Founded in 1993, the group is in the businesses of online drugs; operating a prescription mail order business under its DocMorris brand in Germany, and a market leading online pharmacy business in Switzerland under its Zur Rose brand.

The pharmacy market is ripe for disruption in Europe: small, relatively high value non-perishable packages are extremely well-suited to e-commerce, which remains a very under-penetrated market considering the 125 thousand bricks and mortar pharmacies across Europe which have operated as such for 500 years.

What is more, the German market has recently been prised open by a European Court of Justice ruling and we believe market leader DocMorris will be a key beneficiary.

All-in-all it has been a good year for European equities, and in particular small-caps. But we think they have much further to go: profitability languishes as the earnings of European firms have yet to catch-up to those of their developed market counterparts. In the portfolio we will continue to seek out those businesses that have the potential for superior capital growth over the longer term.

Deflation – a decrease in the price of goods and services across an economy.

Quantitative easing – when a central bank print money to buy assets and stimulate the economy.

Market capitalisation – the total value of a company's issued shares.

Hawkish – policy stance by the central bank aimed at cooling the economy

Capital ratios – the amount of liquid assets a financial institution holds against its risk operations.

Return on equity – the amount of net income relative to the shareholders invested equity.

The above stock examples are intended for illustrative purposes only and are not indicative of the historical or future performance of the strategy or the chances of success of any particular strategy.

The information should not be construed as investment advice. Before entering into an investment agreement please consult a professional investment adviser.

Past performance is not a guide to future performance. The value of an investment and the income from it can fall as well as rise and you may not get back the amount originally invested.

NOW IS THE TIME TO FOCUS ON YOUR INVESTMENT PORTFOLIO

Looking for new companies to invest in? Come and join Shares and AJ Bell Media at their evening event in London on Thursday 19 October 2017 and meet directors from Avacta, Custodian REIT, Non-Standard Finance, Savannah Resources and Xpediator

London – Thursday 19 Oct 2017

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Companies presenting

Avacta (AVCT) Alastair Smith, CEO
Avacta's focus is on its proprietary Affimer® platform technology, a novel engineered alternative to antibodies, that has wide application in diagnostics, therapeutics and research.

Custodian REIT (CREI) Richard Shepherd-Cross, MD
Custodian REIT plc is a UK real estate investment trust, which listed on the main market of the London Stock Exchange on 26 March 2014.

Non-Standard Finance (NSF) Peter Reynolds, Director IR & Communications
NSF's businesses offer credit to the c.10 million UK adults not served by mainstream financial services businesses. Focused on branch-based lending, home credit and guaranteed loans, the Group's goal is to deliver excellent customer outcomes and attractive returns for shareholders.

Savannah Resources (SAV) David Archer, CEO
AIM listed Savannah Resources Plc is a multi-commodity development company focused on building cash generative and profitable mining operations. The Company operates a strategic portfolio of assets, spanning near term production potential and longer term development opportunities in Oman, Mozambique, Portugal and Finland.

Xpediator (XPD) Stephen Blyth, CEO
Recently listed on AIM, Xpediator is the holding company for the Group, a well-established international provider of freight management services operating across the UK and Europe with a particular focus on, and expertise in, the CEE markets.

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Copper explorer SolGold confident of 'world class' project status

Yet company misses an opportunity with its shift to London's Main Market

The boss of copper miner **SolGold (SOLG)** has a message to everyone who has doubted the quality of its assets and management capabilities: 'Ignore us at your peril as we are coming.'

Chief executive Nick Mather says SolGold is building an integrated exploration and development business 'that will rival the world's biggest copper companies'.

That's quite a claim from an exploration business which doesn't even have a resource statement on its project. SolGold is currently valued at £561m and is many years away from generating revenue.

Over-confidence by a CEO is generally a negative sign in the world of investing. However, this boss insists he has every reason to believe his company is far superior to most other mining exploration firms on the stock market.

WHY IS THE CEO SO BULLISH?

SolGold owns 85% of the Cascabel copper/gold porphry project in Ecuador. Drill results from the project have been phenomenal in terms of quality. Mather claims 10 of the 39 holes so far drilled contain 'world class' intersections of continuous copper and gold mineralisation.

If you're not familiar with mining, a project with continuous mineralisation over 100 metres and 1% copper equivalent (copper plus gold valued added together) or better is generally considered to be high quality.

Six of SolGold's drill holes found more than 1,000 metres of continuous copper mineralisation and its best copper equivalent grades are generally between 0.9% and 1.1%. You can now see why Cascabel is a very exciting project. Mather is hopeful the current area being worked (called Alpala) will be one of several high-quality prospects across SolGold's licence area.

More drilling is required on Alpala to check the distribution of the mineralisation in order to create a mine plan. One analyst suggested the full drill programme will take up to five years to complete. Mather says that is nonsense. 'We understand Alpala now. We will drill for another two years to expand it.'

The CEO also rejects suggestions that SolGold won't be in production for another 10 years. 'That is a rate at which a pedestrian major mining house delivers a project. We will be more aggressive due to the high grade core. The earliest we could be in production is four to five years' time,' reveals Mather.

MISSED OPPORTUNITY WITH LISTING CHANGE

SolGold last week (6 Oct) moved from AIM to London's Main Market. Such a move is typically made when a company has reached a certain stage of maturity and wants to be seen as a more credible business.

Companies also tend to graduate to the Main Market when they've reached the appropriate market valuation to qualify for inclusion in one of the two main FTSE indices, being the FTSE 250 or FTSE 100.

SolGold is almost big enough for the FTSE 250 – except it won't be entering the index any time soon. That's something which many investors have failed to grasp, judging by comments on internet bulletin boards.

Tracker funds buy stocks which enter (or are about to enter) the FTSE 250 in order to have an accurate representation of the index's performance. The increased demand for the stock tends to push up the share price.

For example, **Sirius Minerals (SXX)** saw its share price jump by 32% over six weeks after moving from AIM to the Main Market earlier this year.

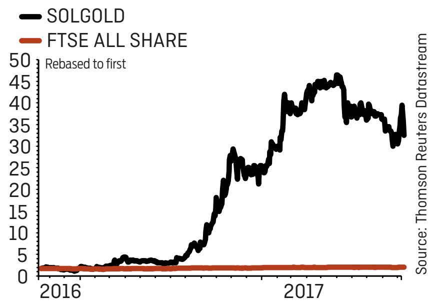
SolGold is different. It doesn't have the right type of listing to qualify for the FTSE 250 so tracker funds won't automatically buy its stock and drive up the price. The miner actually saw its share price fall by 6% on its first day on the Main Market.

In order to qualify, SolGold will need to upgrade from a standard to premium listing. Matthey says it is something that will be considered in the future.

WHY SOME LARGE INVESTORS AREN'T INTERESTED…YET

The lack of a resource statement and any form of feasibility study will act as a deterrent for many institutional investors to be interested in the stock, despite its large market valuation.

SOLGOLD IS 'GETTING A LOT OF INTEREST FROM OTHER MAJORS'



At the moment its biggest shareholders include an investment firm associated with Mather, a mining investment house which owns part of Cascabel and an Asian trading firm. Two other large shareholders are miners Newcrest and Guyana Goldfields. Importantly, stresses Mather, neither miner has a stake at the asset level.

Commenting on Newcrest's involvement, Mather says: 'They provide great technical support and advice on an informal basis. But they don't have any rights apart from the ones that come as a shareholder. They also cannot use their 14.5% stake in SolGold to block any takeover attempts.'

He claims SolGold is 'getting a lot of interest from other majors' and from funds and banks. 'Our strategy is to stay well cashed up.' SolGold had A$89.3m (£49.9m) cash as of 30 June 2017.

FIGHTING OFF INTEREST FROM MAJORS

A year ago **BHP Billiton (BLT)** tried to derail Newcrest's plans to invest in SolGold when it made a proposal to earn-in up to 70% of Cascabel.

'BHP's proposal was poorly structured,' claims Mather. 'The prospective size of the project, plus upside that could be delivered, made it a no brainer to do the work ourselves and reject BHP.'

Sovereign risk is something to watch when considering an investment in SolGold. Ecuador's government is still developing new mining policies. Ten years ago the county imposed a moratorium on mining and implemented a windfall tax, killing the industry.

Ecuador mining is now slowly coming back. 'It's going to be the new porphyry copper province and SolGold will have the best of it,' says Mather, modestly.

He hopes the much-awaited resource statement due later this year on Cascabel will finally give people something to get their teeth into; and start looking at SolGold more seriously. (DC)

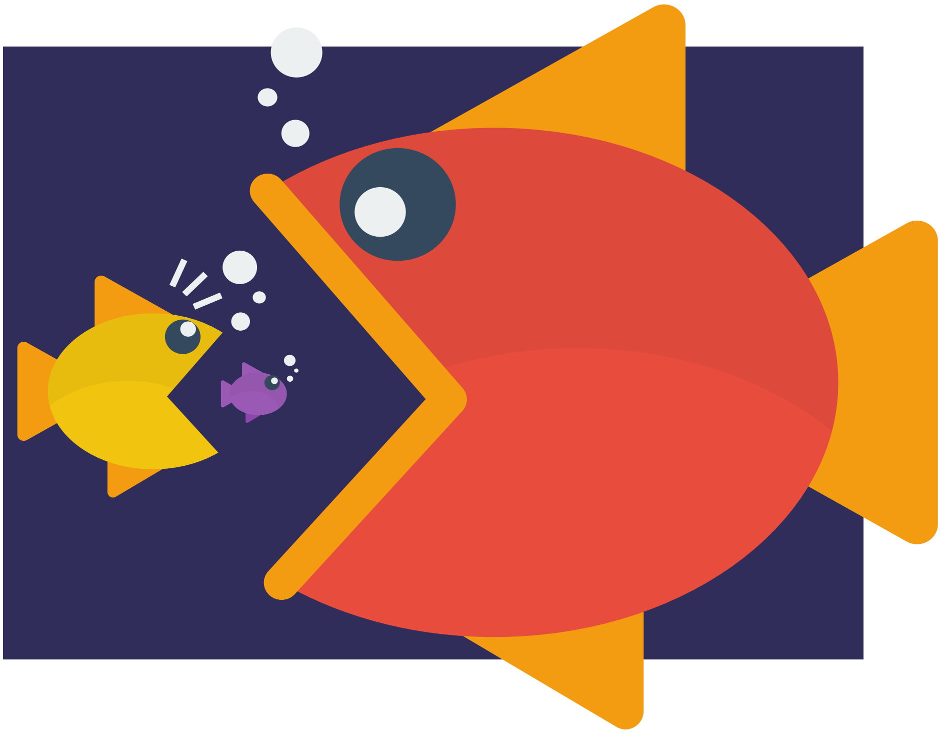
Should I consolidate my pensions?

One pot is easier to manage but transferring could lead to large exit fees

If you've changed jobs several times you've probably got lots of pensions with different providers.

It can be difficult to keep track of how much money you're building up, which makes consolidating your pensions into one pot a tempting option.

But transferring can sometimes result in high charges and the loss of valuable guarantees. It's extremely important to check the terms and conditions of your policies and weigh up the pros and cons before proceeding.



THE PROS

It's a lot easier to manage one pension than it is to manage five. You can see how much money you've saved, there's only one annual statement to read and it's simpler to track and switch investments.

Modern pensions let you see where your pension is investing and how it's performing in real time, so you can figure out if you're on track to meet your financial goals.

Consolidating your pensions can also give you greater control. Alistair McQueen, head of savings and retirement at Aviva, says your current pension may limit your fund choices or, in the case of some trust-based pensions, the trustees may dictate the fund you must have.

If the new pension allows for self-investment you'll have far greater choice. You can pick the investments that suit your individual risk profile and capacity for loss.

> **MOVING YOUR PENSION TO A MODERN ONE COULD REDUCE THE COST OF ADMINISTRATION AND FUND MANAGEMENT**

You could even end up with a bigger pension pot. This is because older pensions often have higher charges, so moving your pension to a modern one could reduce the cost of administration and fund management.

'A small reduction of 0.5% a year might not sound like a lot, but it could increase your eventual pension pot by 15% over your whole working life,' McQueen says. 'Charges are also usually lower the bigger your pension pot is.'

THE CONS

It's not a good idea to transfer a workplace pension in which you are still an active member. Your employer will be paying in money and you'll probably lose this contribution if you decide to stop the pension and transfer it.

Even if you have pensions in which you've stopped contributions, transferring might not be the right decision.

McQueen says that although old pensions generally have higher charges, this isn't always the case.

In addition, some older pensions pay loyalty bonuses, which are added if you keep your pension for a long time. You should weigh up the value of the loyalty bonus against any advantages a new pension would bring, such as lower ongoing charges, more choice and greater flexibility.

Anyone owning a with-profits policy could be subject to a market value reduction (MVR or MVA) charge when transfering out. Phoenix Group says these exist so the true market value of a policy is paid, ensuring the remaining policyholders in the fund aren't disadvantaged.

If you've ever been part of a defined benefit/final salary pension scheme or if you have pensions with guaranteed annuity rates, it's important to check what will happen to these guarantees if you move your money.

If you've got a pension with guaranteed benefits that's worth more than £30,000, you have to take independent financial advice before you move it.

WHAT COSTS ARE INVOLVED?

Some pension providers will apply early exit fees when you transfer out. Jasper Martens, spokesperson for PensionBee, says he's seen some instances where the fee has been in excess of 75% of the pension's value.

Exit fees are becoming increasingly rare but it's worth clarifying with your provider what the charges will be.

You may also incur financial advice fees and the less obvious cost of time out of the market.

'During the time between the old plan closing and the new plan starting, the money won't be invested anywhere so people could lose out on market increases. Of course, the opposite is also true – they could benefit from falling markets,' explains Jamie Clark, a business development manager for Royal London.

> "IT'S A LOT EASIER TO MANAGE ONE PENSION THAN IT IS TO MANAGE FIVE"

HOW LONG DOES A TRANSFER TAKE?

Transfer times can vary hugely. Thornton Wells, wealth management consultant at Mattioli Woods, says some insurance-based contracts transfer in a matter of days whereas older contracts can take weeks.

Some providers use an industry standard transfer process called Origo. It takes around six to eight weeks, but if the providers have good service levels and it's not a complex case it can take eight days.

WHAT ELSE DO I NEED TO CONSIDER?

There are lots of things to think about before transferring to another pension.

Look at whether the new pension offers the investment choices you want and all the options you need, such as regular income withdrawals, ad-hoc withdrawals and the ability to view and change your investments online.

Analyse the charges. McQueen says some pensions have a single fee whereas others have fees for taking income withdrawals, buying and selling investments and buying an annuity.

'You should consider the charges you will pay depending on how you plan to use your new pension, both now and in the future,' he adds.

Other factors to consider include whether the provider has an exit fee and what their customer service is like.

HOW DO I CONSOLIDATE?

Once you've chosen a pension call the new provider and ask them if they offer a service that helps you consolidate your pensions.

Most will write to existing providers on your behalf to get the necessary paperwork, so all you have to do is sign and return the forms. Once you've returned the forms, the transfer can go ahead. (EP)

Should I quit my defined benefit pension scheme?

We run through the essential points to consider

Tens of thousands of savers have ditched the security of a defined benefit (DB) pension since the launch of pension freedoms in April 2015. This type of pension usually pays out a guaranteed, inflation-linked sum in retirement.

Individuals have switched in favour of managing their own retirement pot through a defined contribution (DC) scheme such as a self-invested personal pension (SIPP).

With a report by influential trade body the Pensions and Lifetime Savings Association (PLSA) suggesting 3m members in the weakest DB schemes have only a 50/50 chance of getting their full pension; this demand is unlikely to ease any time soon.

Furthermore, many savers are attracted to the extra flexibility created for DC savers by the pension freedoms and the ability to pass on funds tax-efficiently after death.

But the process of transferring is not straightforward and comes with real risks.

SEEKING FINANCIAL ADVICE

If you want to transfer your DB pension and it's valued at £30,000 or more, Government rules require that you speak to a regulated financial adviser first. You can search for an adviser near you on www.unbiased.co.uk.

Financial advice is extremely valuable – particularly in relation to complex areas such as pension transfers – so it's worth listening carefully to what they tell you.

Advice doesn't come cheap. According to adviser search provider Unbiased, specialist defined benefit transfer advice costs around £1,500.

Even if you're willing to pay that, many advisers simply aren't taking on pension transfer business either because they don't have the qualifications or they fear being sued further down the line.

TRANSFER VALUES

An adviser will talk you through a whole series of issues that factor into whether or not a transfer is right for you.

One of these is the transfer value – this is the cash amount your DB scheme is offering you to give up your guaranteed pension.

The size of the offer will depend on a number of factors including your age, whether your pension is inflation-proofed and the yield (that is investment return) on Government gilts (if the yield is low, the transfer value will be high). Your transfer value will be expressed as a ratio.

For example, if you have a DB pension worth £10,000 a year and you're offered a transfer value of 20:1 you'll get £200,000 in exchange for giving up your guaranteed pension.

Clearly such cash offers are extremely tempting but remember you'll be giving something up that's incredibly valuable. DB pensions usually come with inflation protection – meaning the real value of your income will be maintained – and also often guarantee to pay your spouse an income after you die.

IS THE SCHEME SPONSOR SAFE?

In light of the PLSA report you might be concerned the company that's supposed to pay your DB pension won't survive as long as you do. This is perfectly logical but it's worth noting that even if the scheme sponsor hits the wall you won't be left empty handed.

The Pension Protection Fund (PPF) provides a valuable safety net for DB members in the event their employer (or ex-employer) fails.

If you have already retired and were receiving a pension from your scheme before it went bust, the PPF will pay you 100% compensation. You'll get the same level of retirement income as when the scheme you're a member of failed.

Payments relating to pension rights built up from 5 April 1997 will rise in line with inflation, subject to a cap of 2.5%. Payments relating to service before then will not increase.

If you retired early and had not reached your scheme's 'normal pension age', or had yet to retire, when your employer went bust, you'll generally receive 90% of the income you would have received.

However, this is also subject to an annual cap on compensation depending on how old you were when you retired. The PPF maintains a list of cap levels for each age. The earlier you retired,

> WHETHER OR NOT TO TRANSFER WILL DEPEND ON YOUR OWN PERSONAL CIRCUMSTANCES AND GOALS.
>
> WHATEVER YOU DECIDE, REMEMBER THAT YOUR PENSION FIRST AND FOREMOST NEEDS TO PROVIDE AN INCOME THAT LASTS THROUGHOUT YOUR RETIREMENT – A PERIOD THAT COULD LAST 30 YEARS OR MORE

the lower the annual cap set to compensate for the longer time you will be receiving payments.

For example, the cap at age 65 is just short of £35,000 a year (when the 90% compensation level is applied).

Payments will increase with inflation in the same way as someone who has already retired.

So in short, while the failure of the company that is supposed to pay your pension will reduce your retirement income, you should still get most of it.

WHAT DO YOU WANT FROM YOUR PENSION?

Whether or not to transfer will depend on your own personal circumstances and goals. Some people will already feel they have enough secure income to fund their day-to-day spending and are therefore able to cash-in the rest (although remember this will be taxed in the same way as income).

Others will be attracted to the tax treatment of DC pensions which allows you to pass on your entire fund tax-free if you die before age 75 or at your recipient's marginal rate if you die after this age. Furthermore, you can now pass it on to anyone – it doesn't need to be a spouse or dependant.

Whatever you decide, remember that your pension first and foremost needs to provide an income that lasts throughout your retirement – a period that could last 30 years or more. In most cases, keeping your DB pension will remain the best way to do this.

Tom Selby,
Senior Analyst, AJ Bell

Tesco's titanic turnaround

We're sticking with the grocer as Dave Lewis' strategy literally pays dividends

Supermarkets giant **Tesco's (TSCO)** impressive half year results (4 Oct) confirmed its eagerly-anticipated return to the dividend list after a three-year hiatus. We'd hang on for further gains from the grocer's turnaround, although we acknowledge the shares have rebounded strongly since June and concerns over a planned £3.7bn merger with wholesaler **Booker (BOK)** remain.

DIVIDEND RESUMPTION

The £15.43bn cap's half year results proved a milestone, a modest 1p payment demonstrating confidence and CEO Dave Lewis guiding towards a 3p full year dividend. Pre-tax profits surged from £71m to £562m, operating margins rose to 2.7% and are on track to hit the 3.5-4% target range by 2019/20, while net debt reduced 25.1% to below £3.3bn.

Tesco's sales inflation in the half was around 1% less than the rest of the market, helping it attract customers back in droves. Ketan Patel, co-fund manager of the Amity UK fund, explains: 'As Tesco has the largest market share of 28%, it can afford certain buying powers and can invest these savings into pricing to keep up with the hard discounters.'

In the UK and Republic of Ireland (ROI) business, like-for-like sales grew 2.1% for a seventh consecutive quarter of positive performance. We're hoping to see continued progress when Tesco reports on Christmas trading (11 Jan 18).

BOOKER – POTENTIAL BANANA SKIN?

Nevertheless, the medium-term outlook remains uncertain given cut-throat competition between the big players and Aldi and Lidl. The Booker merger is going through the machinations of the UK Competition & Markets Authority (CMA) and some believe Booker could prove a banana skin.

'However, should it go ahead, we believe the deal presents good value for Tesco,' counters Patel. 'The merger will position Tesco as a supplier to the eating out industry and convenience, both of

which offer superior growth compared to the food at home its store base serves. As the largest UK food retailer, Tesco can leverage its scale to cut costs, reinvest in pricing and remain a competitive player and this acquisition will help increase scale.'

UBS has a 'buy' rating and 270p 12-month price target that implies 45% upside. For the year to February 2018, analyst Daniel Ekstein forecasts material earnings improvement to 10.56p (2017: 6.32p), ahead of 13.48p in 2019, where a 3p dividend should rise to 5p per share.

TESCO'S PAYING DIVIDENDS (AGAIN)

Financial years to February	Dividend per share
2015(A)	1.6p
2016(A)	0p
2017(A)	0p
2018(E)	3p
2019(E)	5p
2020(E)	8.73p
2021(E)	9.24p
2022(E)	9.6p

Source: Company accounts, Thomson Reuters, UBS estimates

SHARES SAYS: ↗

At 186.5p, Tesco trades on a fulsome 17.7 times forecast earnings, although with the stock in recovery mode and Lewis' strategy paying off, we're sticking with the global grocer. (JC)

BROKER SAYS: 6 7 7

Investors 'regaining favour' with mining exploration

Boss of newly-listed Cora Gold implies there is hope for pre-revenue natural resources firms

Institutional investors are slowly regaining interest in mining exploration stories, according to the boss of a newly-listed gold explorer.

Jon Forster says he was impressed at the reaction to **Cora Gold's (CORA:AIM)** IPO (initial public offering) marketing roadshow, given that the exploration side of the mining sector has been deeply unloved for the past four years.

Forster, who is CEO of Cora, admits that having a link to **Hummingbird Resources (HUM:AIM)** did help its cause when trying to raise cash ahead of its stock market debut on 9 October.

Cora secured £3.45m in new money to help advance a variety of prospects including assets previously owned by Hummingbird in West Africa.

Hummingbird is in the middle of building the Yanfolila gold mine in Mali. It recently decided to streamline its portfolio to primarily focus on development work and sold some exploration interests to Cora in exchange for becoming an investor in the business. Hummingbird now owns 33.85% of Cora.

Some of the exploration assets now in Cora's portfolio could potentially become sources of ore to be processed at Yanfolila by Hummingbird. Initial drill work has found promising levels of gold and further drilling is required to better understand the ore body.

Coinciding with work on these prospects will be further drilling on Cora's flagship property called Sanankoro in southern Mali.

FTSE 100 miner **Randgold Resources (RRS)** and South African producer Gold Fields have previously explored the property, providing Cora with substantial amounts of historical data although not enough to form a resource statement. Forster says Cora is hoping to prove up 1m ounces of gold across the four permits which make up Sanankoro.

The third leg to the Cora story involves two exploration projects called Diangounte and Madine Fulbe in Mali, near the border of Senegal. Forster believes Diangounte could be a future supply of ore for AngloGold Ashanti's Sadiola gold mine which is located 6.5 kilometres away, should further exploration prove the asset is worth developing.

Madine Fulbe is a joint venture with SN Minerals which hasn't complied with the terms of the exploration licence. The breaches of the legal and contractual obligations present a risk that SN loses the licence, says Cora.

It is also worth noting that many of Cora's exploration licences are relatively short-term in nature and some have already expired and are awaiting renewal.

Shares in Cora fell by 3.8% to 15.88p on its first day on the stock market. We believe investment group Glenwick was behind the selling. It acquired Cora stock in the summer as settlement for costs associated with a cancelled reverse takeover of the mining business. (DC)

The life insurer with a difference

GBGI operates in niche markets and has a heavyweight partner

Guernsey-headquartered **GBGI (GBGI:AIM)** is a life insurance company that also offers cover for private medical treatment, disabilities and travel.

Its global footprint makes this company stand out; Angola is one of its strongest markets and it operates in 120 jurisdictions via a global network of representatives.

GBGI is a mix of insurer and managing general agent, the latter meaning it writes unusual lines of insurance which require specialised expertise.

Using analyst Canaccord Genuity's forecasts, GBGI trades on 9.4 times 2018's 18.7p of earnings while paying a dividend yield of 6.4%.

GBGI's cash position more than doubled between 2014 and 2016 from $24.6m to $53.8m respectively. Canaccord concludes that 'the history of GBGI's cash flow implies that conversion of profits to cash has been fairly high and consistent'. This provides confidence on the dividend.

Given its product diversity and geographical spread, there are also plenty of growth opportunities for the company. It could benefit from trends such as global labour mobility and increasing middle classes in emerging markets for example.

French insurance giant AXA partners with GBGI acting as the company's reinsurer for its health business and will also cover life and disability from January 2018.

In exchange for GBGI's reinsurance business, AXA has agreed to cross sell business back to the company, act as a fronting partner and assisting the company in getting upgraded by insurer rating firm AM Best.

Canaccord has a price target of 200p, implying about 14% upside at the current 175.5p. (DS)

RedstoneConnect moves on

SMART BUILDINGS solutions designer **RedstoneConnect (REDS:AIM)** has batted-off a bizarre takeover approach.

AP Systems announced a plan to buy RedstoneConnect on 28 September without contacting the company directly.

Having since received a formal letter, RedstoneConnect has binned the proposal because of the lack of detail. No valuation was mentioned, calling into question AP Systems' intentions. (SF)

Sound Energy exits Italy with Saffron deal

AFTER AN unsuccessful result from its Badile well (3 Jul), oil and gas focused company **Sound Energy (SOU:AIM)** is spinning its Italian assets into **Saffron Energy (SRON:AIM)**.

Sound Energy will now focus on its Moroccan portfolio while Saffron is combining with its main shareholder Po Valley Energy to create Coro Energy. Coro will be chaired by Sound CEO James Parsons and Coro shares will be distributed to Sound shareholders. (TS)

Datatec adds up cash return

INVESTORS COULD be in for a huge cash windfall from IT solutions business **Datatec (DTC:AIM)**.

The company is expected to confirm a $500m value return when it reports half year results on 13 November.

That could be worth 180p per share if it was all handed out in cash, although a share buyback plan is expected to also be part of the capital return. The shares trade at 325p. (SF)

KEY

- **Main Market**
- **AIM**
- **Fund**
- **Investment Trust**